No technology, no matter how amazing (...) can by itself ignite a shift from good to great. (...) People are absolutely essential. (...) People, however are not an organization’s most important asset, the right people (with the right values, attitudes and behaviors) are an organization’s most important asset.

Jim Collins, Good to Great

Many managers were over-exposed in impressionable childhood years to the story in which the imprisoned, enchanted prince is released from the toad’s body by a kiss from the beautiful princess. Consequently, (when considering a merger,) they are certain that the managerial kiss will do wonders for the profitability of the target company. Such optimism is essential. Absent that rosy view, why else should the shareholders of company A want to own an interest in B at a takeover cost that is two times the market prices they’d pay if they made direct purchases on their own? In other words, investors can always buy toads at the going price for toads. If investors instead bankroll princesses who wish to pay double for the right to kiss the toad, those kisses better pack some real dynamite. We’ve observed many kisses, but very few miracles. Nevertheless, many managerial princesses remain supremely confident about the future potency of their kisses, even after their backyards are knee-deep in unresponsive toads.


M&As: Can’t live without them, but you might not survive them

In 1996 PricewaterhouseCoopers conducted a nationwide study of 124 recently merged companies and found that the objectives that drove the transaction were met only half the time and often took years to be realized. This was congruent with the results of an exhaustive analysis of hundreds of deals led by Business Week, which concluded that even those that were several years old hadn’t begun to work. Of 150 deals valued at $500 million each or more, about half actually destroyed shareholder value and another third contributed only marginally. Further, the least-achieved objectives had often been the most sought after, such as reductions in manufacturing costs, distribution costs, and operating expenses.

More recently (Nov. 2003), Business Week reported on a study performed by McKinsey on what they called “the merger-fest of 1998.” During that year, there were a large number of high profile deals such as Citicorp-Travelers, Conseco-Green Tree, Bank One-First Chicago, NationsBank-Bankamerica and Daimler Benz-Chrysler. The results were not encouraging: seventeen out of the twenty one mergers led to great losses for the shareholders of the acquiring company.

Seventeen out of the twenty-one mergers led to great losses for the shareholders of the acquiring company.

Some of the reasons reported were: the premiums paid were too high, the managers didn’t understand what they were buying, the synergies they envisioned were an illusion, they severely underestimated the costs of consolidating the operations of companies with different cultures, and they didn’t know how to prevent the loss of key employees, salespeople and customers.

“The track record of mergers and acquisitions is abysmal,” conclude Feldman and Spratt—authors of Five Frogs on a Log. “When it comes to M&A, it’s remarkable how much money and time is spent and how much commitment a CEO makes to buy a company and how little is spent to make it work. Frequently, much more cash goes to goodwill than to human resources, marketing and product development. After the announcement is made, management typically awakens to

By Fred Kofman and Albert Durig
the cold reality that strategy and execution are two different animals. As a senior executive reported, “buying is fun; merging is hell.”

A trip to hell seems in store for those who are lured by the promises of cost reduction. The previously mentioned PricewaterhouseCoopers survey found that reductions in operating expense is the fourth most frequently targeted M&A objective (by 28 percent of respondents). However, it is the eleventh most frequently achieved (15 percent of respondents). As Feldman and Spratt remark, “Reducing costs invariably proves more difficult than anticipated. On the surface it appears to be a simple matter of eliminating duplication and reducing unnecessary overhead. However, the extraction of cost requires fundamentally altering work processes and procedures, redeploying people, making additional investments in training, and coping with the demoralized and overworked workforce that remains after others are laid off. Reductions of productivity of 20 to 30 percent are not uncommon, easily offsetting the paper gains that were anticipated as a result of downsizing.”

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On the other hand, the upside is enormous. As the Fortune article “Why CEOs Are Learning to Love Mergers” reports, “competing in a global economy takes scale and scope. This is what’s behind the mega mergers of the 1990’s and many of the strategic alliances. On a more incremental basis, there is the matter of growth: many small high-tech businesses need capital to grow, and more-established firms need these start-ups to grow their top line—hence the record number of acquisitions in high tech and other growth fields. And there is the matter of leveraging competencies and technologies. Modern markets are giving birth to “cooperative competition,” whereby companies may compete with one another in some arenas while simultaneously taking steps toward a partnership, the eventual acquisition by one another, or a spin-off business that is then sold to a third firm. In either case, what better way to prospect in a new market area, gain some know-how, and make some money?”

Whether for product or service diversification, vertical integration, globalization, risk sharing, access to technology and resources, operational complementarities, innovation and learning or consolidation, companies have an irresistible drive to join forces. On the other hand, companies are finding that the dream team they envision the night before the merger becomes a nightmare the morning after.

Socio-Technical Systems

Most researchers and authors on the subject understand the socio-technical nature of organizations. They realize that beyond processes, systems and structures, organizations are collections of human beings. So in their writings they devote considerable attention to the “human dimension”. Issues of communications, team building, goal alignment and others related to large scale change appear with prominence.

For example, in Joining Forces, Marks and Mirvis state upfront that “human and cultural dynamics encumber every combination.” They identify the key tasks for implementing a value-creating merger as: “refining a winning strategy for the combination, aligning the new organization behind it, building a culture to support it, and getting people to deliver desired results.” They report that the most frequent barrier to accomplishing these tasks is “power and politics, which intrude on every decision and subvert attempts to create value.”

Feldman and Spratt report that in the 1996 PricewaterhouseCoopers survey, 49 percent of the respondents reported differences in operating philosophy as the most troublesome post-deal difficulty. Moreover, cultural differences were perceived to have incurred substantial costs in terms of lost business opportunities. The same year, in a change management survey conducted by the Wall Street Journal (Europe), 54 percent of the respondents reported that culture was the main obstacle they encountered in implementing change. “Invariably,” conclude the authors, “culture appears at the top of everyone’s problem list. Cultural differences in operating style, customer relations, and communications represent formidable obstacles to post-merger integration.”

... companies are finding that the dream team they envision the night before the merger becomes a nightmare the morning after.

Saying that “culture is a great hindrance” is a self-defensive way of saying “we don’t understand culture, and we don’t know how to respond to the challenge of cultural change and integration.” Just like a weight that’s “too heavy” for me, is “light” for Arnold Schwartzenegger, the cultural problem is “difficult” for most managers because they don’t understand it, and are not competent to deal with it. The good news is that if I practice diligently and grow my muscles, the weight will “miraculously” become lighter. By the same token, if managers develop themselves and become more skilled in the cultural dimension, their problems will become less difficult.
Culture

Culture is a set of characteristic behaviors, derived from a collection of shared values and beliefs. Every community develops its own culture as a way of systematizing successful responses to the challenges it has faced in the past. This “knowledge” is codified in the unconscious of every member, enabling them to make the most routine decisions in his or her life without having to involve the more expensive “CPU” resources of rationality and calculation. Life would be unmanageable if we had to think through everything we do moment by moment. But the blessing of an automatic process that is effectively adapted to historic circumstances becomes the curse of an automatic process that is unable to cope with new circumstances, with change.

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Few circumstances in the business realm create more structural change than merging with another company. Each organization’s business processes, protocols, values, lexicon, expectations, pain thresholds, walk and talk, even humor, are hard-wired through traditions created by and familiar to those who share them. These behaviors and mental models cannot be re-wired in a hurry. Mergers can take months, even years to plan. Making the new combined entity an organic whole, can take even longer. Cultural integration requires the creation of a new shared understanding and new shared practices. This requires the deactivation of many automatic processes that helped a company respond in the past. In fact, these previously successful processes, when not actively changed, can become a “leaden life-saver”.

Researchers have found that there is no adjustment of behaviors among two different populations simply because they are in contact. Thus, cultures won’t merge without a design effort. It’s an illusion to think that this will occur naturally and gradually through a process of recurrent interactions. This “contagion approach” has proved ineffective in almost every experiment and study performed by social scientists. The business world is full of failed experiments of this kind.

For example, AOL’s acquisition of Time-Warner turned disastrous ultimately resulting in the resignation of the formerly acclaimed CEO, Steve Case. Equally painful was AT&T’s failed attempt to get into the computer business by acquiring NCR. Even IBM was humbled by its failure to penetrate the telecommunications business with its bid for and subsequent selling of Rolm. Equally difficult is to “merge” one’s way into the mainframe computer business, as Xerox’s failed merger with Scientific Data Systems demonstrates. All these failures derive (amongst other reasons) from a clash of cultures that could not be overcome. Analyzing this last example, Harvard Business School’s David Yoffie said, “There was a terrible clash of cultures. Xerox was unable to integrate Scientific Data’s highbrow computer specialists with its own blue-collar copier technicians.”

Equally ineffective is the approach predicated on the belief that culture can be changed by preaching vision and values. The platitudes preached are like motherhood and apple pie. Simply put, cultures can’t be changed by passionate sermons, off-sites, incentive systems, newsletters, screen savers, or posters.

Espousing values via these methods misses the point. The real issue is whether these values are manifested through the executives’ actions day in and day out. If not, they are merely rhetorical ideas that never get put into practice. AOL/Time-Warner, AT&T/NCR, Compaq/Digital Equipment, and hundreds of other failed combinations who spent millions of dollars in “values campaigns” are all proof that most often it’s the latter.

Cultures can’t be changed by passionate sermons, off-sites, incentive systems, newsletters, screen savers, or posters.

Behavioral Recommendations

After recognizing the critical nature of the human factor, experts move on to offer recommendations. Some of the reasonable policies they propose include the following:

1. Basing the transition on the economic value drivers, and accelerating it to reduce the pain (“the law of the band-aid”).
2. Convincing managers to work together as a team and to act first on those things that drive shareholder value.
3. Developing an aggressive integrated communications strategy that addresses stakeholders’ concerns, builds on their hopes, and speaks to them through channels they trust, in terms they can understand (“no secrets, no surprises, no hype, no empty promises”).
4. Launching small transition teams sponsored by a member of the executive team as soon as possible.
5. Designing an organization (and an organizational chart) towards the optimization of performance, not the accommodation of ego.
6. Reengineering work processes, roles and responsibilities to align them with business priorities.
7. Selecting and deploying role models who support the desired culture.

8. Designing incentive systems that focus attention and resources on the creation of shareholder value.

These recommendations are useful. They can yield good results when implemented. But the problem with these suggestions is that they disregard the consciousness and psychological make-up of the persons that have to execute them. If there is no supporting platform (infrastructure) of values and mental models in each individual, no matter how good the process, it will not work.

It is easy to see this with a computer analogy. If one tries to run Microsoft Office XP on a Windows 95 operating system, it will not work. The problem is neither in the application programs nor in the operating system, but the combination of the two incompatible elements. By the same token, it is not enough for a manager to understand the benefits, believe in and even be committed to an attitude of acceptance of diversity. If he or she has a brittle and defensive personality structure, no conscious attempt to remain open to the other company’s culture will succeed when he or she is confronted with potentially threatening situations.

The problem is neither in the application programs nor in the operating system, but the combination of the two incompatible elements.

Psychologists talk about behaviors that are “ego-dystonic” or “ego-syntonic”. Ego-dystonic behaviors are those which don’t mesh with one’s mental model (core beliefs about oneself, others, and the world). If we push our example, we could say that Office XP is dystonic for Windows 95. Ego-syntonic behaviors are those that fit one’s mental model. For example, an aggressive response to a disagreement is ego-syntonic for a narcissistic “know-it-all”. As described in “Knowledge, Learning and Power”, a know-it-all is a person whose self-esteem is based on being right, somebody who feels that he or she must “save face” at all costs and never be proven wrong in public.

Individuals and organization are reluctant to abandon old habits. Conscious beings possess strong defense mechanisms that resist change. That’s why the first step of any cultural change includes dealing with the “immune system” that protects individual and collective mental models from “foreign” ideas.

Cultural Integration and Change

Cultural integration and change is about behavioral change, not rhetoric. Statements of vision and shared values are only a starting point. The real engine of cultural change is the observable behavior of highly visible executives and leadership teams. The problem of cultural integration is not intractable, it’s just badly mismanaged. Time, contact, and internal communication campaigns are insufficient tools. To change and integrate cultures it is necessary to address the behavioral dimension. And the best way to do this is through a combination of role modeling and training.

First, the company needs to define the desired behavior that if shared across the newly merged entity, will result in achievement of business goals. The good news is that there are many behaviors already proven to drive success in the achievement of business goals. Some of these behaviors include: acting with unconditional responsibility with an emphasis on regular evaluation of one’s role and impact on surrounding business circumstances, staying calm under pressure, effectively managing and resolving conflict, confronting the brutal facts regardless of the pain involved, speaking the truth and not harboring “undiscussables”, discovering someone else’s truth, and making effective complaints without personal blame.

These behaviors by themselves do not create change unless applied with discipline. Desired behavior must be disciplined behavior. As stated by Jim Collins, “People, are not an organization’s most important asset, the right people (with the right values, attitudes and behaviors) are an organization’s most important asset.” The company needs to select “the right people” who exemplify these desired behaviors in a disciplined manner and deploy them in visible positions of authority. In doing so, they become cultural role models. The only reliable way to accurately identify “the right people” (cultural role models) is to include behavioral interviewing and simulation testing in the candidate screening process. Without the data provided by these techniques, executives risk being blind, forced to “bet the farm” on a leadership team selected on the basis of technical skill, inferences, politics and personal preference.

But having “the right people” is only part of the equation. The company then needs to be generous and public with its recognition of their performances. This will clearly signal that the path to success is in emulating these behaviors. People have to want to change. They will only want to change when they see that it is in their best interest to do so. Therein lies the importance of recognizing and rewarding individuals that emulate culturally desired behaviors. Without “the right people” being recognized openly for all to see, companies will confuse inconsistencies that send mixed messages to the rest of the organization and effective cultural change will not occur. But even employees motivated to change are not enough to achieve cultural change. Employees need to learn
how to behave as those cultural role models they desire to emulate.

Providing employees with tools that will enable them to think, feel and behave like “the right people” is essential. When people feel the incentive to change and emulate the role models, it is necessary to support them with cognitive-behavioral training and coaching. For example, staying cool and thinking clearly in the face of problems is easier said than done. Some people have a natural ability, but most need to develop their skill through practices that train not only their minds, but also their hearts and bodies. The same is true for speaking honestly and respectfully when conveying potentially threatening information. Even if one wants to do it, it is necessary to incorporate (from the Latin, “put in the body”) the actionable know-how (not just the informational know-that). This incorporation process demands off-line acquisition (such as what can be accomplished in a workshop), on-line application under supervision or support (such as what can be offered by a coach) and off-line reflection and error-correction (such as what can be done in coaching sessions or team reviews).

Finally, it is important to avoid contradictory messages that put people in double-binds and undermine cultural change and integration. This occurs regularly when there is a contradiction between a company’s written policies and the behaviors it rewards. For example, a company can claim that quality is its priority but reward employees only for the quantity produced, regardless of quality. Or it can preach teamwork, but reward only individual performance. Or it can encourage employees to be innovative and take risks, but then reprimand them for not following established procedures and worse, punish them for failing. No matter what the company’s official position is, people operate according to the refrain: “what you do speaks so loudly, that I cannot hear what you say.”

It is important to avoid contradictory messages that put people in double-binds and undermine cultural change and integration.

The Ice Cube Model

In the 50’s the social psychologist Kurt Lewin proposed a simple model of organizational change: unfreezing, changing and refreezing. “Suppose that your target for change is not an organization or an individual, but an ice cube,” suggest Marks and Mirvis, “If you want to convert the cube to a cylinder, you can proceed in one of two ways. The first is to use a hammer and chisel. You might succeed, but there’s a clear cost to this approach: you lose a good amount of ice. The alternative is to unfreeze the cube, change its mold to that of a cylinder, and refreeze it.” When executives tackle M&As with chisels and hammers, the economic and social consequences are not pretty. The acquirers see themselves as conquerors, and insist that targets conform to their bureaucracy—regardless of any consideration about relative efficiency or cultural traditions. Political gamesmanship runs rampant, with management teams fending off others’ attempts to wrestle control away from them. Cultural clashes lead to turf wars and a siege mentality. Everybody hunkers down to protect their territory, and nobody minds the system as a whole. Under those circumstances, people perceive integration activities as a threat, a “waste of time” that distracts them from their “real work.” They are blind to the vital few—adding critical success factors, so they don’t put any energy or focus on them. Furthermore, everybody pays a high emotional price. Stress and anxiety disorders, de-motivation, depression, substance abuse and general health problems increase significantly during merger episodes.

... people perceive integration activities as a threat, a “waste of time” that distracts them from their “real work.

So common are these problems that they have been given a name: Merger Syndrome. According to the theory, there are three types of reactions to merger stress: 1) Personal reactions, such as preoccupation, worst-case scenario anxiety, rumor-mongering, distraction, risk aversion, survivor guilt and psychosomatic reactions; 2) Organizational reactions, such as crisis management, centralization, miscommunication, combat mentality, inter-group tension and group-think; 3) Cultural reactions, such as clashes, versus-they mentality, win-lose negotiation tactics, and decisions by coercion, horse trading and default.

Under these conditions, it is no wonder that the field of mergers and acquisitions is littered with—metaphorically and literally—dead bodies.

Unilateral Control and Productivity Killers

In our twelve years of experience with individual and organizational change, we have identified a set of productivity killers which are derived from an obsolete mental model—we call it unilateral control (see “From Unilateral Control to Mutual Learning”). In order to develop productivity enhancing behaviors, it is imperative to “upgrade” the individual and organizational culture towards a mutual learning orientation.

We can apply the theory of productivity killers to M&As and highlight the gap between “the wrong people” (those who can’t inspire an effective cultural integration, maximizing
economic value and the human development) and “the right people”. The “wrong people” display wrong values, wrong attitudes and wrong behaviors:

Wrong Values

- Integrity subordinated to success: “I will do anything to win,” is one of the most dangerous commitments one can make. It implies that one is “a transgression waiting to happen.” There are universal values that foster long-term health—economic, social and psychological. Those who betray them sow evil seeds of (self-)destruction.

- Ego-centrism and selfishness: Trust is a function of service. When people believe that their manager is trying to “use” them for his or her own personal benefit without regard for their well being, they don’t feel used, they feel abused. Those unable to “walk in someone else’s shoes” and offer “value in return of value” generate ill will and resentment around them.

- Unconscious reactivity and emotional immaturity: “An unexamined life is not worth living,” said Socrates. If a person does not have the capacity to reflect about themselves and develop emotional maturity, he or she will act inconsistently. We all have contradictory impulses within ourselves. Those who don’t develop the capacity to manage them will be managed by them.

Wrong Behaviors

- Destructive communication: Most managers oscillate between brutal honesty (“that’s a stupid idea”) and hypocritical respect (“that’s an interesting idea, but I don’t know if it is the best alternative...”). They spend all their time advocating for their position, without any interest in listening (and inquiring into) other people’s perspectives. These patterns create lots of undiscussables, which choke the organization’s capacity to get valid information about its situation and act effectively.

- Conflict escalation: Diversity can be the source of great creativity, but only when people know how to manage it. When the managers of different organizations get stuck on their positions as a way to assure their narcissistic fears, they cannot find creative solutions to synthesize the knowledge. Those that cannot transcend their ego driven tendencies are totally unable to integrate diverse perspectives in a more encompassing point of view.

- Lack of implementation: Coordination of action happens through a dance of requests and (fulfilled) promises. When people make careless or unclear commitments, when they operate with no regard for their “creditors”, and when they neither fulfill nor renegotiate their promises, the organization falls into a state of paralysis. Those who lack integrity around commitments are like a cancer that destroys trust, thus disabling an organization’s ability from turning decisions into actions. On the other hand, the “right people” possess different and value-adding values, attitudes and behaviors:

Right Values

- Integrity is the only way to success (no compromises).

- Service orientation and care (concern for every “other”).

- Consciousness and equanimity (non-reactivity, awareness and choice).

Wrong Attitudes

- Know-it-all with Blame-ability: Arrogance is a show-stopper for any team effort. When people are stuck on defining their positions simply to show they are “right”, they forget completely about being effective. Those who love their face more than the truth—and thus try to save the former at the expense of the latter—are a great liability for any organization.

- Innocent Spectator: The price of innocence is powerlessness. When people defend their self-esteem by attributing whatever goes wrong to causes outside their control, they automatically disable themselves to take corrective action—after all, it’s out of their control! Those who don’t see themselves as part of (and able to respond to) the problem, cannot see themselves as part of the solution.

- Reactive Victim: Resignation and resentment are pervasive in a culture of victim-hood. Self-disempowered victims feel at the mercy of external circumstances. Those who fall prey to this tranquilizing story, poison the emotional well of the organization.

Right Attitudes

- Learner with response-ability (able to respond “in the face of” any circumstance).

- Engaged player (powerful, capable of deciding how to tackle any challenge).

- Committed author (enthusiasm and peace since everything and anything is an opportunity to express his or her greatness).
Right Behaviors

• Essential honesty (naturally respectful) and humility; ability to balance skillful advocacy with skillful inquiry and making everything discussable.

• Creative negotiation, focused on the satisfaction of everybody’s concerns and interests.

• Impeccable commitments, honored with unconditional integrity—through fulfillment or renegotiation with concern for and care of the creditor.

Conclusion

Children’s tales, such as the Frog and the Princess, reveal deep personal and cultural archetypes. Carl Jung, a contemporary of Freud, devoted his life to understanding how myths reflect and shape the unconscious of individuals, communities and even humanity as a whole. He found it fruitful to interpret these stories as dreams where each character symbolizes an aspect of the personality of the dreamer. One’s own self is the single actor in the dream, taking different roles to enact the play.

Turning frogs into princes is not something that can be done from the outside. To help some frog become a prince, it is useless to kiss it. The frog, the prince and the kissing princess, all exist within the same psyche.

What can be done is to help the self-deluded frog discover its true princely nature. Transformation is “an inside job,” it can be helped, but not “done” by some external force.

That’s why the leaders of merged companies have so much trouble with cultural change and integration. They are trying to mandate the changes from the top down and the outside in. They see themselves as change agents. (Would you like to be changed by a change agent? Not me! Perhaps we should have a dictum: “Change agent, change yourself!”) Moreover, most leaders talk the talk, and many of them may even want to walk it; but the overwhelming majority has no legs to do so. Being a role model implies that the integration has already happened within. The most powerful thing a leader can do is show the transformation taking place within him or her. That will inspire others. Once the desire is in the others’ hearts and minds, the main job of leadership is to provide a supportive environment which balances developmental challenges and generous training.

Mergers and acquisitions are like earthquakes. They shake the ground, and with it, the illusion of stability. During turbulent times, people feel like they’re at sea, without anchor or moorings. Managing day-to-day operations in such an environment is a tremendous job; even more difficult is to lead the integration of business systems, cultures and personalities. No wonder most mergers sink! To reach a safe harbor, everybody (starting with the leaders) needs to develop the necessary “sea legs” to walk the talk, as well as the values, beliefs and behaviors required to execute the strategic vision that inspired the combination. Paraphrasing Jim Collins, we can say that only “the right people” have a prayer of making it through the stormy seas of M&As, people that have awakened to their essential nature, and are ready to support others through that process.

The Merger Syndrome is a special case of the very human anxiety-response to the uncertainty of life. Unless companies develop leaders that can respond more confidently to the impermanent nature of reality, all the technical and behavioral recommendations in the world are useless. To reduce the personal and economic costs of a merger, and to enhance its value, it is necessary to find, develop and empower those that have confronted their deepest fears, that have gone through the fire of transformation, have found their spiritual truth, and are ready to let it shine as an exemplar for others.

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