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Five Guidelines to Prevent Failed Cross-Border Deals

By Anthony Bahr

Over the past decade, there has been a drastic increase in both the number and the value of cross-border mergers and acquisitions. Today, cross-border deals account for roughly 40% of global M&A activity, and there is little evidence to suggest this trend has plateaued as acquirers continuously evaluate new growth and diversification opportunities outside of their home markets.

Unfortunately, it is well documented that most of these deals fall short of expectations. Failure rates are pegged anywhere between 70% and 90%, leaving only a handful of deals that actually enhance shareholder value. What is less documented however, are the underlying causes for failed cross-border M&A activity. “Integration issues” are commonly cited, but what does that really mean? And how can acquirers structure due diligence to reduce the chance of failure?

A recent survey of Fortune 500 CFOs found that one of the most critical components of a successful integration is “customer retention and expansion”. The same survey also found this to be one of the most challenging integration aspects to manage.

Based on our experience conducting customer due diligence on behalf of global private equity firms and strategic acquirers, we have developed five guidelines for improving customer retention and expansion in order to increase the odds of a successful cross-border deal.

1. Determine the degree of customer loyalty.

One critical component of a customer diligence initiative is the Net Promoter Score® (NPS®) to determine if a customer is a “Loyal,” “Passive,” or “Detractor.”

Our clients are often surprised to find that among their top quartile of customers by revenue, a majority fall into the Passive segment, meaning they are somewhat satisfied but not necessarily loyal or willing to refer the business to a colleague. More concerningly, we frequently find a handful of top customers are Detractors; they report serious barriers to satisfaction and are at risk of leaving for a competitor.

The implications for acquirers are two-fold. First, the fact that top revenue generators are at risk of either lower share of wallet (Passives) or pulling their business outright (Detractors) has a material impact on Quality of Earnings estimates, which should make acquirers think twice about the target company’s valuation.

Second, assuming the deal closes, acquirers should immediately address the concerns raised by Passives and Detractors during the diligence process in order to retain these critical accounts.

2. Verify the company is providing a consistent customer experience.

A cursory analysis of customer feedback in total may not reveal the whole truth. Weaknesses in the customer experience that could eventually result in lower share of wallet or attrition are often only identified through a more in-depth analysis of the findings.

Therefore, when designing a customer diligence program, considerable attention should be paid to the number and distribution of interviews. Having the ability to analyse customer feedback by various segments (region, for example) is critical to ensuring the target is providing a consistent customer

experience. Plus, the ability to analyse customer feedback by mutually exclusive segments empowers acquirers to develop more precise and prioritised post-close strategies and tactics to boost loyalty.

3. Ensure the target is highly engaged with their top accounts.

In business-to-business deals, personal relationships are paramount. This is because people tend to do business with other people, and it is why a customer’s level of satisfaction with their primary contact tends to be highly correlated with their satisfaction toward the company itself.

But beyond their day-to-day contact, customers also desire senior-level attention. We find this to be especially true in cross-border deals, since customers often seek reassurance that a global integration will not disrupt business as usual or their standing with the target company.

Through the customer diligence process, acquirers can determine which accounts warrant more engagement, while also providing management with customer-level feedback to guide effective engagement planning and execution.

4. Benchmark a target company’s performance against key competitors.

Quantifying feedback through the NPS® and other metrics is useful when gauging customer perceptions toward a target company, but it is easy – and dangerous – to fall into the trap of interpreting data without comparative perspective.

This is especially true in cross-border diligence since cultural nuances can impact the way in which customers respond to questions.

This is why effective customer diligence should include a competitive benchmarking exercise. For example, a NPS of +45 might be considered a “good” score, but if the target company’s primary competitor receives a NPS of +60, then acquirers should be less confident in the company’s position. Having this point of comparison helps put findings in context, while also neutralising any response bias attributed to cultural differences.

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5. Validate the future growth potential of the target company.

Since a majority of value creation is attributed to revenue growth, and since the primary motive for M&A deals is to maximise value creation, then it follows that acquirers should want to validate the revenue growth potential of a target company during the diligence phase.

Perhaps the most effective way to accelerate revenue growth is to innovate. Unfortunately, we have seen many instances where a target company has invested heavily in an innovation pipeline without ever asking the customer if the new feature or service has any practical application. Hence, it should be of little surprise that so many new product launches fail.

If having a clearly defined problem is the first step in developing a truly breakthrough innovation, then methods which take the voice of the customer into account are more likely to uncover opportunities that will generate demand. A recent example: we partnered with a leading manufacturer of specialty chemicals and, during customer interviews, we identified over 200 potential new innovation opportunities.

More so than domestic deals, cross-border transactions are fraught with risks. Fortunately, smartly designed and executed customer diligence can mitigate several of the most common risk factors, while also providing insights to accelerate value creation post-close.

Anthony Bahr is a Vice President in Strategex's Voice of the Customer Strategic Practice, where he leads research-based consulting engagements.

Anthony devotes much of his time to expanding the firm's Quality of Customers® (QofC®) offering – a proprietary process that incorporates voice of the customer research into customer due diligence pre- or post-close on behalf of private equity and strategic acquirer clients.

He works in partnership with clients to design and implement research initiatives to address common questions that arise during the due diligence process, and provides insights into a customer's level of satisfaction and loyalty, as well as competitive positioning, innovation pathways, and pricing optimisation.

Before joining Strategex, Anthony held senior-level positions at two leading market research firms where he specialised in insight, strategy, and innovation projects for global financial services, consumer packaged goods, and pharmaceutical clients. He is well versed in multiple methodologies including brand positioning, segmentation, advertising effectiveness, and pricing optimisation.

A veteran of the United States Air Force, Anthony holds a B.B.A. in economics and international business from Loyola University Chicago as well as graduate degrees from the University of Oklahoma and University of Chicago.