THE SYNERGY CHALLENGE – TEN KEY ACQUISITION LESSONS LEARNED: THE CASE OF MERCURY COMPUTER SYSTEMS AND MYRIAD LOGIC

By Bob Becker

Copyright Management Roundtable, Inc. 2007

THE SYNERGY CHALLENGE – TEN KEY ACQUISITION LESSONS LEARNED: THE CASE OF MERCURY COMPUTER SYSTEMS AND MYRIAD LOGIC

By Bob Becker

It seems like it should be easy. If we acquire company XYZ, combine revenue and then, on top of that, realize some of the many additional potential synergies between personnel, products, processes, and systems we'll do very well. Before the acquisition we make estimates of those synergies and we bake them into the price we pay. There is a great deal of data to suggest that most acquisitions are not successful in meeting the original goals that seemed so achievable beforehand.

While I was the Senior Vice President of Engineering and Operations at Mercury Computer Systems, we acquired five relatively small companies in the span of three-and-half years. In each of those instances, Mercury was looking for complementary capability that would enable the combined entity to provide a new, unique solution to our customers. The business cases always included accretive revenue at some point and some additional synergies beyond the new market potential of future products. We got smarter with each one. In early 2002, Mercury completed the acquisition of Myriad Logic, which became our 'IO Center of Excellence' (IOCE). Four years later on the heels of a small corporate business downturn the site was closed. This article focuses on what went right and wrong in the case of the first of those acquisitions.

For the sake of argument, even assuming that the business downturn was unavoidable, the decision to throw in the cards probably was not. There was value in the talent of the acquired organization, but it never seemed to reach the potential we not only hoped but planned for. Here's the punch line – realizing the synergies too slowly created a cycle of underinvestment that ensured that the original business upside we expected would never be met. After spending millions on the purchase, it was doomed to miss expectations by choices made early on.

If a positive view of the potential opportunity led to the acquisition, how did that, in turn, lead to underinvestment and eventual closure in just a few years? Naivety is too simple an answer.

There was a great team that worked very hard to make sure action was taken very quickly.

- *Payroll and (mostly) improved benefits were in place on day one.*
- *We immediately integrated their two-person sales team with a much larger, worldwide sales force and began a program of incentives to try to focus scores of salespeople to sell the new product set.*
- *We conducted a significant internal PR campaign to try to make sure that corporate folks would be helpful whenever called upon to assist at the IOCE.*

With the advantage of hindsight, we can see that other well-intentioned decisions were driven by a fear of what could go wrong.

- *We put handcuffs on the acquired company's founder because we were afraid that if he left, the institutional knowledge and customer relationships associated with him couldn't be*

replaced and many of the 30 employees would soon follow. He was in for large bonuses after a couple of years if he could grow that business substantially.

- *We didn't try to integrate the acquired engineering team with corporate R&D – as a matter of fact, we tried to leave them alone – for fear of imposing our larger company overhead on a more entrepreneurial, remote team. We correctly understood that the cultures were quite different.*
- *We waited for several quarters before beginning to replace their unsophisticated ERP system with our state-of-the-art Oracle system for fear of major production hiccups with their products since their business processes were very different from our own.*
- *We waited a year-and-a-half to consolidate their manufacturing operation into the corporate operation for fear that there was magic sauce that we might not understand and every revenue dollar was too important to risk. We were also afraid that we would alienate the engineering team when their production colleagues went thru workforce reductions.*

Everyone involved worked hard to make the acquisition a success. A concerned management team also tried to do no harm to this important, newly acquired asset.

So what happened?

Let's start with the leadership of the acquired company. As it turns out, the Founder/CEO turned VP/GM resigned and retired a year-and-a-half later despite the handcuffs we had applied. Besides the difficulty that an entrepreneur faces when becoming a part of a much larger organization, there were more fundamental problems that we created from the start. First of all, the strategic intention was that this was a product group whose products would be integrated with the corporation's in order to create a new, compelling system. Yet, the leader was named GM and compensated based on growing an independent business. That implementation was counterproductive in terms of the changes needed to achieve the strategic goals.

In addition, we took away the GM's small but dedicated sales force, integrating them into a large team selling a broad set of products. As it turns out, these new, lower priced products were difficult for the big team to sell and left them with smaller commissions for their time despite the incentives that were offered to them. That left the GM with no channel that he could control to drive the sales growth on which his incentives were based. Ultimately those growth incentives became a frustrating disincentive.

The delays in consolidating ERP systems led to having more than one set of books. The last thing corporate finance wanted was to put substantive investment into a part of the business where the numbers were suspect. Due to the lack of visibility, a lot of time was wasted arguing about details rather than realizing the strategy.

Maintaining a redundant manufacturing operation meant that when one looked at the IOCE as a standalone business, it was expensive to run. All the corporate norms and systems for how investment funds were allocated were stacked against adding dollars for R&D; those R&D dollars were needed to evolve the product family – to either grow it as a business or achieve some of

the strategic goals by working on new products with the rest of the corporation. Before the savings from merging the IOCE manufacturing operation into the corporate operation were realized, low R&D investment had effectively turned the IOCE into a sustaining engineering group, unable to afford to add any new value in the form of innovative new products.

While trying to leave the IOCE R&D separate from corporate R&D was well-intentioned, it led to unanticipated ill effects. While corporate waited for the IOCE to create IO product strategies, the IOCE wanted to please Mercury and awaited product direction. Corporate expected a degree of aggressiveness that was the norm elsewhere in the company while the newly acquired organization awaited direction from the new bosses.

The lack of interaction between the organizations also meant that the IOCE personnel tended to waste a lot of energy whenever they had to figure out how to navigate any corporate system. About 6 months into the acquisition we realized that this problem was easy to overcome by locating a well-connected person from the corporate engineering team at the IOCE for six months, ostensibly to help them get ready for ISO certification. This local connection worked incredibly well.

In summary, some well-intentioned choices were made that got the operation out of sync with the strategy; frustrated the workforce and leadership alike with a lack of clarity and inconsistent direction; stymied R&D investment due to expense levels and visibility issues; and eventually resulted in those people and assets being some of the first jettisoned when times got tough.

Ten key lessons from this story include:

1. IF YOU ARE NOT PUTTING YOUR OWN LEADERSHIP IN PLACE IN THE ACQUIRED FIRM, CREATE A SUCCESSION PLAN – ESPECIALLY IF IT'S A FOUNDER WHO NOW HAS BOSSES TO DEAL WITH.
2. MAKE SURE THAT STRATEGIC OBJECTIVES STAY IN THE FOREGROUND DURING THE FLURRY OF ACTIVITY DURING AND IMMEDIATELY FOLLOWING THE ACQUISITION.
3. CHECK TO BE SURE THAT THE AUTHORITY AND RESPONSIBILITY OF KEY FIGURES ARE ALIGNED, ACCEPTED AND UNDERSTOOD.
4. BE CAREFUL WITH LOCKING-IN LONG TERM INCENTIVES WHEN THERE ARE MANY UNKNOWNS SINCE IT TAKES MANY OPTIONS OFF THE TABLE.
5. BE CAREFUL HOW YOU COUNT – IT'S A STRATEGIC CHOICE THAT COLORS ALL DECISIONS.
6. IDENTIFY AN ENGAGED, CORPORATE EXECUTIVE TO PAY ATTENTION AND USE THEIR CLOUT TO REDIRECT CORPORATE FUNCTIONS OUT OF 'BUSINESS AS USUAL' MODE IF NEEDED.
7. PUT CORPORATE FEET ON THE GROUND AT THE NEW SITE, FULL TIME FOR AT LEAST AS LONG AS IT TAKES TO ASSIMILATE THE NEW GROUP AND ACHIEVE A LEVEL OF COMFORT FOR ALL INVOLVED.

8. INVEST TO MAKE INTER-SITE COMMUNICATIONS AS EASY AS POSSIBLE – ORGANIZE THE WORK TO MINIMIZE THE NEED TO USE IT.
9. WORK OUT THE INTERFACES EARLY FOR WHO, WHAT AND HOW TO DO BOTH TACTICAL AND STRATEGIC DECISION MAKING.
10. IF FEAR CAUSES YOU TO PLAY NOT TO LOSE, YOU WON'T WIN. DO THE WORK TO HAVE CONFIDENCE, MAKE CHOICES AND EXECUTE. [MRT]