

Abstract: M&A activity tends to wax and wane. Nonetheless, billions of dollars continue to change hands annually, and an acquisition can be a great way to grow a business. So owners should be prepared if one of these deals comes their way. This article explores some pros and cons to consider.

Why you should (or shouldn't) pursue an acquisition

Like so many aspects of the national and global economies, merger and acquisition (M&A) activity tends to wax and wane. Nonetheless, billions of dollars continue to change hands annually, and an acquisition can be a great way to grow a business. So if one of these deals comes your way, it's important to carefully consider both the pros and cons.

Look at the possibilities

Merging with, or acquiring, another company is one of the best ways to grow rapidly. You might be able to significantly boost revenue, literally overnight, by acquiring another business. Achieving a comparable rate of growth organically — by increasing sales of existing products and services or adding new product and service lines — can take years.

An acquisition also might enable your company to expand into new geographic areas and new customer segments more quickly and easily. You can do this via a horizontal acquisition (acquiring another company that's similar to yours) or a vertical acquisition (acquiring another company along your supply chain).

In addition, you can realize synergies by acquiring the right type of company. Synergies are business characteristics and capabilities that complement and work well with those of your own company. The idea is to find an acquisition target that offers the right synergies so that the new combined entity will be stronger than either business would have been on its own.

Be aware of drawbacks

Although there are many potential benefits to acquiring another business, there are some potential drawbacks as well. For example, completing an acquisition is a costly process, from both a financial and a time-commitment perspective.

Therefore, you should determine how much the transaction will cost and how it will be financed *before* beginning the M&A process. Also try to get an idea of how much time you and your key managers will have to spend on M&A-related tasks in the coming months — and how this could impact your existing operations.

A loss of control is another potential drawback to consider. Depending on the deal's structure, some degree of control may have to be shared with the owners of the business you're acquiring, especially if the owners aren't retiring but intend to be actively involved with the merged entity.

It's also critical to try to ensure that the cultures of the two merging businesses will be compatible. Mismatched corporate cultures have been the main cause of numerous failed mergers, including some high-profile megamergers. For instance, if one company has a more formal and buttoned-down culture while the other is more casual and laid back, conflicts will likely ensue unless you plan carefully for how the two divergent cultures will be blended together.

Perform due diligence

The best way to reduce the risk involved in buying another business is to perform solid due diligence on your acquisition target. Your objective should be to confirm claims made by the seller about the company regarding its financial condition, clients, contracts, employees and management team.

The most important step in M&A due diligence is a careful examination of the company's financial statements — specifically, the income statement, cash flow statement and balance sheet. Also scrutinize the existing client base and client contracts (if any exist) because projected future earnings and cash flow will largely hinge on these.

Finally, try to get a good feel for the knowledge, skills and experience possessed by the company's employees and key managers. In some circumstances, you might consider offering key executives ownership shares if they'll commit to staying with the company for a certain length of time after the merger.

Map your course

An acquisition is one way to expand and grow your company. But be sure to map your course thoroughly before heading down the M&A road. Our firm can help steer you in the right direction.

© 2017