

Achieving M&A Success in the 'New Better' Requires Aligning People Risk and Financial Risk

As employers adapt their human capital strategies to address issues exposed by the COVID-19 pandemic, they should also examine how they manage emerging human capital risks during M&A. We explore areas of people risk that will drive the success of transactions.

One of the many realities that was reinforced during the COVID-19 pandemic is how vital a firm's human capital strategy and management is to the business success of an organization. Organizations that were able to quickly pivot to remote working and equip managers with the tools to lead remote teams, for example, were better positioned to respond and recover from business disruption. This is one of the many reasons why shareholders are increasingly interested in companies' human capital management (HCM). In the United States, that heightened interest is reflected in mandatory disclosure of HCM in companies' annual reports beginning in 2021.

Companies now need to translate their focus on (and enhanced disclosure of) HCM to M&A transactions — the success of which is often hinged on the ability to effectively integrate human capital.

The complexity of managing corporate transactions has been often discussed. There is strong agreement among business leaders and practitioners that effectively integrating teams based on a sound due diligence process is the most important critical success factor of a transaction. With around half of all modern M&A deals deemed a failure, an examination of internal factors often points to missed synergies, inadequate due diligence process and a lack of cultural alignment.

In order to assess how to better integrate human capital, let's look at the main purposes of M&A transactions. Deals normally are to drive financial capital (e.g., business bolt-on, product extensions) or brand capital (e.g., companies build platforms or enter adjacencies that they can sell to their existing client base). Rarely do firms consider the human capital they are acquiring until after the first two considerations have been satisfied. However, through our experience in advising clients during transactions, human capital is rightly becoming a bigger consideration and success factor. That's partly because many recent deals are technology or intellectual property-driven transactions. For these deals, the acquirer is paying a premium for talent that is in high demand in the labor market. We expect to see more of these types of deals as companies develop workforce strategies to drive productivity and reshape their business for a post-pandemic future.

Below we suggest some new focus areas for businesses involved in transactions that are based upon emerging human capital risks. These considerations are intended to encourage companies to ask how "future-ready" the different workforces are that will be coming together.

Figure 1

New Focus Areas for M&A Integration Based on Human Capital Risks

Risk Area	Traditional Transaction Focus	New Focus
Workforce demographics	<ul style="list-style-type: none"> Assess potential demographic gaps Review the mix and legacy of the workforce 	<ul style="list-style-type: none"> Comparison of workforce mix to future skills Mix of digital talent and comparison to top companies Diversity of workforce
Workforce capabilities	<ul style="list-style-type: none"> Leadership capabilities that will drive transaction objectives Pivotal employees that will drive business results 	<ul style="list-style-type: none"> Agility of leadership team Resiliency of workforce Reskilling needs (and related budget) to ensure a future-ready workforce
Total rewards	<ul style="list-style-type: none"> Risks related to HR programs, mostly in retirement, health and benefits, as well as executive compensation 	<ul style="list-style-type: none"> Total rewards alignment to new ways of working Effectiveness of total rewards
Culture	<ul style="list-style-type: none"> Potential culture gaps and their impact on the transaction objectives 	<ul style="list-style-type: none"> Alignment of culture to the agile way of working Embracing new workforce models (e.g., hybrid model) Inclusivity of the culture
Retention	<ul style="list-style-type: none"> Focus on leadership 	<ul style="list-style-type: none"> Focus on a future-ready critical workforce
HR policies	<ul style="list-style-type: none"> Policies that support a high-performance culture 	<ul style="list-style-type: none"> HR policies that support new ways of working and provide a positive employee experience Consideration of environmental, social and governance (ESG) and diversity and sustainability targets in the performance system

Next Steps

Human capital is a complex risk that is becoming more influential during M&A transactions. With growing recognition that people-related risks can negatively impact both brand and financial capital if not properly managed, we encourage business leaders to ask the types of questions we lay out in the table above. The standard risk areas will remain valid in future transactions, but by adding a more future-orientated view of addressing these risks, companies are in a better position to address human capital integration early on.

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