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# M&A

## AS A STRATEGIC OPTION

FROM OPPORTUNITIES  
TO NEW BUSINESS  
CREATION

The Federation of Finnish  
**Technology  
Industries**

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# PREFACE

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This book is the outcome of a research project entitled ManMAP<sup>1</sup> (Managing the M&A process – from opportunities to new business creation (2009–2011)). The focus of the project was on the process of new business creation (NBC) through merger and acquisition (M&A) activity. The overall objective was to enhance understanding among researchers and practitioners of how activities related to the creation and acquisition of new business converge, and how the related strategic decision-making could be managed successfully.

The ManMAP project was conducted through an inter-disciplinary research consortium consisting of Turku School of Economics (TSE) and VTT Technical Research Centre of Finland (VTT). Research on M&A is very lively and versatile at TSE, and spans departmental boundaries from international business to accounting and finance. M&A expertise in this research rests primarily on the post-acquisition integration process. VTT is a multidisciplinary organisation specialised in technology and technology-based business research, with specific emphasis in this research on risk and innovation management, technology foresight and strategic-planning processes, and evaluation techniques that support NBC-related decisions. This book is based on the contributions of researchers from both TSE and VTT.

The ManMAP project and this book would not have been possible without the financial support of several parties. Both have been funded by The Finnish Funding Agency for Technology and Innovation (Tekes), TSE, VTT and the ManMAP project's case companies – Outokumpu Oyj and Tieto Oyj. The editors wish to express their gratitude to all of the above. They also give their sincere thanks to all the researchers at TSE and VTT involved in the project and in the writing and finalising of this book. However, our deepest gratitude is owed to the 28 people and 14 companies – Elisa Oyj, IBM Corp., Itella Oyj, Nokia Siemens Networks, Tieto Oyj, Oy Karl Fazer Ab, Cargotec Oyj, Kone Oyj, Metso Oyj, Kemira Oyj, Orion Oyj, Outokumpu Oyj, Rautaruukki Oyj and Yara International ASA – who allowed us to carry out the interviews during the autumn and winter of 2009–2010. Your contributions are invaluable.

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<sup>1</sup> ManMAP is a Tekes-funded collaborative project involving Turku School of Economics and the VTT, Tieto Oyj and Outokumpu Oyj. For more information please visit <http://www.vtt.fi/manmap>.

Finally, we give our warmest thanks to **Hanna Masala** from Outokumpu Oyj, **Tom Nikander** and **Ilkka Korkiakoski** from Tieto Oyj and **Ismo Matinlauri** from Cargotec Oyj for the interesting discussions and their valuable comments on the manuscript. We are also grateful to our colleagues **Lotta Häkkinen** and **Niina Nummela** from TSE and **Helena Kortelainen** and **Pekka Maijala** from VTT for their insightful comments during the writing process. Last but not least, we wish to express our deepest gratitude to **Joan Nordlund** for the comprehensive language check, and to **Eira Yrttiaho** from Teknologiainfo Teknova Oy for her input and editorial support starting from the initial phases of the writing process and ending with the publication of this book.

31.5.2011

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# 1 CREATING NEW BUSINESS THROUGH ACQUISITIONS

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## 1.1 Why Did We Write This Book? Experiences from the ManMAP Project

Increasing competition and globalisation force firms to grow, internationalise and find new business opportunities. New business is expected to create growth as well as to increase the competitive strength of the company. However, the creation process may be challenging. The situation is even more complex in the context of mergers and acquisitions (M&A)<sup>2</sup>. New business creation (NBC) may require one large acquisition, or a number of smaller ones. Success depends largely on how well these acquisitions are managed and integrated.

Although acquisition activity has shaped industries and organisations for decades, never has it been pursued in such magnitude as during the past decade or so. However, it is not just the sheer volume of contemporary M&A activity that makes the phenomenon highly topical, but also the spread. Acquisitions are becoming common in industries and markets that, until recently, have been relatively untouched by such restructuring. Furthermore, companies are operating in an increasingly global, dynamic and turbulent environment in which it is imperative to find new ways of doing business in order to survive and remain competitive. The recent financial crisis is a case in point: it has created turbulence in the market, which may open up very lucrative business opportunities for some and put others under serious pressure to consolidate. M&A activity decreased dramatically following the credit crunch and the financial crisis: in 2008 and 2009 cross-border M&A decreased by 34 per cent, and the drop in value was 65 per cent (see also Table 1). However, recent figures indicate a growth trend in 2010.<sup>3</sup>

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2 Although mergers and acquisitions are used interchangeably, true mergers are rare. Moreover, the concept of a merger is often used as a synonym for integration (cf. Lees 2003). M&A is used in this book as a general concept to refer to acquisitions.

3 World Investment Report, 2010

**Table 1. Value of cross-border M&A purchases by industry during 2000–2010 (\$ billion)**

(Jan – May)	2005	2006	2007	2008	2009	2010	2011
Total	462	625	1023	706	250	339	224
Primary	3	32	95	53	29	53	39
Manufacturing	119	164	218	245	38	120	79
Services	340	429	710	408	183	166	106

(Source: UNCTAD, [www.unctad.org](http://www.unctad.org))

The link between acquisitions and the exploration of emerging business opportunities has become more salient during the past decade. For example, companies such as Nokia, Unilever, Siemens, Bertelsmann and Intel have set up various types of venturing programmes that typically include business development through acquisition. This also highlights a shift in the understanding of innovation from something that happens at the heart of the company in dedicated R&D units to an activity that is more pervasive and open in nature. Companies in Europe operating in the fields of information technology, energy, business services and consumer goods, as well as media and lifestyle businesses, have been particularly affected by this trend<sup>4</sup>.

Given that business renewal is a key to long-term success, NBC is a highly strategic issue. Companies have to find a balance between using their existing strategies to assess opportunities and exploring the potential of new business to redefine their strategic focus<sup>5</sup>. It is less likely that they will be successful in the future if they go on too long with strategies that meet current needs. Furthermore, the very process involves taking a step towards an unknown future, and uncertainty with regard to the related decision-making. Uncertainties related to new markets and new technologies complicate matters further, given the need to take into account the differences in time span. Whereas markets may change quite rapidly, for example, the creation of new business through organic development could last for years. Acquisition activities introduce additional risks arising from the possibility that key personnel will leave or fail to co-operate. Consequently, the decision to acquire a new type of business requires particularly careful consideration given the high level of risk.

4 EVCA Annual Survey..., 2007; Reichardt & Weber, 2006; see also Buckland et al., 2003.

5 Terwiesch & Ulrich, 2008

M&A could be seen as one potential coping mechanism in a business environment in which the new initiatives, knowledge and insights that are innovation prerequisites come from individuals and organisations anywhere in the world, within the company or from outside<sup>6</sup>. In this context, M&A and related search and scanning activity aimed at identifying and creating new business are not individual and isolated events: it is a profoundly strategic issue. However, the contexts in which business creation and acquisition are combined can differ. Examples include:

- *Technology and product-oriented companies seeking new growth opportunities in the service sector*
- *Mature industries searching for new markets with future strategic relevance*
- *Turbulent business environments in which traditional structures and player roles are in flux or converging*
- *Companies buying innovation to complement or even replace traditional in-house R&D.*

It may be virtually impossible in such contexts to predict how profoundly entire industries and markets may change as a result of certain emerging technologies or societal trends. Moreover, a company's whole set of goals may change over time. Such settings characterised by multiple uncertainties raise numerous questions in terms of strategic decision-making when the market for the potential business does not yet exist, for example<sup>7</sup>. Furthermore, the future strategic importance of the acquired business may be highly uncertain at the time of the acquisition.

The challenges companies engaging in this type of acquisition face are largely different from those addressed in the majority of the M&A literature. For example, the differences in time-related aspects and in the relationship between acquiring and acquired organisations, as well as between the internal and the external business environment call for new approaches to the M&A process. Extending the research into these areas through the ManMAP project will support companies with regard to finding and creating new business opportunities, developing models for coping with conditions of high uncertainty, and taking a more future-oriented approach in related activities.

The aim of the ManMAP research project was to bring new insights into NBC management through M&A activity. The project included four more specific objectives:

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6 Birkinshaw & Hill, 2005

7 See e.g., Sarasvathy, 2001 on decision-making in the case of entrepreneurial contingency

- Acquiring a comprehensive understanding of risk management across the whole NBC and M&A process from design to business continuity
- Acquiring a comprehensive understanding of the related strategic-decision-making process in the same context
- Acquiring a comprehensive understanding of timing in this process, and of how it could be made more future-oriented
- Providing support for companies attempting to build up a successful process in terms of the three previous objectives (identifying critical decisions and providing tools for coping with conditions of high uncertainty, for example).

The research project was conducted in cooperation with several major Finnish companies. A total of 24 interviews were conducted in 14 large Finnish enterprises (see Appendix 1), mainly with M&A directors, although some were with integration managers and other M&A experts within the organisations. The 14 companies in question have vast M&A experience in terms of both growth and internationalisation. They represent several business fields, and vary in size, in terms of the strategic motives behind the M&A and in geographical market area. The results describe various approaches and best practices in the different phases of the process, from the identification of new business opportunities to the integration of the acquired company and evaluation of the M&A.

In sum, the aim of the ManMAP research project, and consequently of this book is twofold: (1) to provide information on and insights into the creation of new business through mergers and acquisitions, in other words to discuss a) how to support the related strategic planning and decision-making, b) how to incorporate uncertainty into the planning processes, c) how to develop a strategic view of M&A in terms of implementation and d) how to integrate new business opportunities successfully; and (2) to introduce practical methods and tools to support the management of this process. Whereas the traditional literature focuses on describing and defining the M&A and integration processes, this book is *more strategy-oriented in terms of providing insights and tools covering the period from the recognition of the opportunity to its implementation through M&A.*

## 1.2 What Is It All About?

The ManMAP framework in Figure 1 below illustrates the M&A process from the perspective of creating new business, which requires a strategic vision and proactive procedures, and the ability to identify and evaluate new opportunities and to align them with the strategy. Companies need to be able to define relevant scenarios concerning not only how the business markets will evolve but also how future technologies will affect them. The ManMAP framework demonstrates the link between opportunity management and NBC with the corporate strategy and vision, as well as the process of implementation through acquisitions and integration of acquired business. This framework constituted the concrete base on which the ManMAP research project was built, which is reflected in this book.



Figure 1. The ManMAP framework for creating new business through acquisition

Creating new business through mergers and acquisitions is very challenging, especially in the light of the poor success rate, which remains mediocre at best. It has been argued that around 50–75 per cent of M&A fail<sup>8</sup>. Several acquisitions may be required, and the integration process may be challenging if it remains unclear how the new business will turn out. The ManMAP framework comprises three major building blocks, namely Opportunity Management, New Business Creation through M&As and Business Continuity Management.

<sup>8</sup> Marks & Mirvis, 2001; King, Dalton, Daily & Covin, 2004; Schoenberg, 2006

*Opportunity management* emphasises the role of strategic planning: the direction in which the company intends to take the business. In recent years, companies have placed more emphasis on the development of formalised processes to support NBC. The recognition and evaluation of new business opportunities is not easy, however, and it may be even more difficult when it is a question of business renewal in a mature company. Further problems include the vast amount of inadequate data available during the early phases of the process, and the uncertainty not only about the new business in question, but also related to the consequences of failure. The challenge for management is to determine how much uncertainty is acceptable, and to assess and evaluate it. The development of a realistic new-business implementation plan is also an essential element of the strategic-planning process and thus of profitable business growth. Different strategic alternatives, including alternatives to M&A, should be evaluated and thoroughly discussed.

*New business creation through M&A* emphasises the proactive nature of acquisition, which is motivated by the need to create new business. The majority of acquisitions occur within the same industry and in related business fields, but the creation of new business requires risk taking and stepping out of the comfort zone. Selecting and evaluating the target are much more challenging, for example. In addition, integrating the business may take longer given the need for a great deal of knowledge transfer and learning between the acquirer and the acquired company.

*Business continuity management* emphasises the role of effective integration, and also of feedback in reassessing whether the new business is in line with the strategic objectives. Business continuity represents the most challenging part of the framework. For instance, it may take years before synergies are realised. An effective feedback system is needed throughout the integration phase in order to manage the M&A process successfully and ensure the continuity of the newly merged entity. However, the system seldom extends beyond the integration efforts exerted for each acquisition individually, and may not analyse in sufficient depth the success of the whole project in line with the company's strategic ambitions.

The framework provides an integrated approach to M&A. In other words, it views M&A as the result of overall corporate strategic planning, and as merely a tool with which to implement the strategy – a means to an end<sup>9</sup>. Its main contribution lies in the deep integration of the whole process into the corporate strategy, and the fusing of the deal-making (pre-M&A)

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<sup>9</sup> cf. Bower, 2001

and integration (post-M&A) phases through an effective feedback system. The linking of NBC and M&A also has major implications for practitioners, especially in terms of being proactive even in turbulent market situations such as the recent financial crisis, and taking a strategic approach to the search for new business opportunities.

Structured strategic-decision-making and opportunity management processes and methods may be useful management tools in this respect. It has been argued that in conditions of rapid and significant environmental changes, companies must continually compare the costs, payoffs and risks of achieving the requisite adjustments independently with the terms and conditions of exit<sup>10</sup>. Consequently, risk-conscious decision-making forms the basis of the integrated framework, from the recognition of the new opportunity, through the creation of the new business through M&A to business continuity management. The deeper the integration of opportunity management, the M&A process and the related decision-making, the easier it is for executives to manage the uncertainties inherent in the process and thus to maximise the company's sustainable value. From the perspective of risk and opportunity management, the benefits and risks of the new business should be considered in the relation to the many and various stakeholders who will be affected.

### **1.3 How This Book Supports the Process of New Business Creation through M&A and Target Readership**

The purpose of this book is to support companies in their aim to create new business through M&A. From this perspective it will enhance the capability to plan and manage the process and support the related decision-making in a systematic and strategic manner. The procedures described are not tied to any branch of industry. However, the subject matter concerns, in the first place, large companies planning to expand their business through M&A. The book is aimed at all managers and people involved in strategy and business development, investment planning and the M&A process, from business-unit to board level. It gives strategic insights on both the corporate and the business-unit level, and offers tools for M&A teams and managers involved in the concrete integration work. Figure 2 below and the paragraph following it guide the reader through the book and explain the structure.

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<sup>10</sup> Conklin, 2005

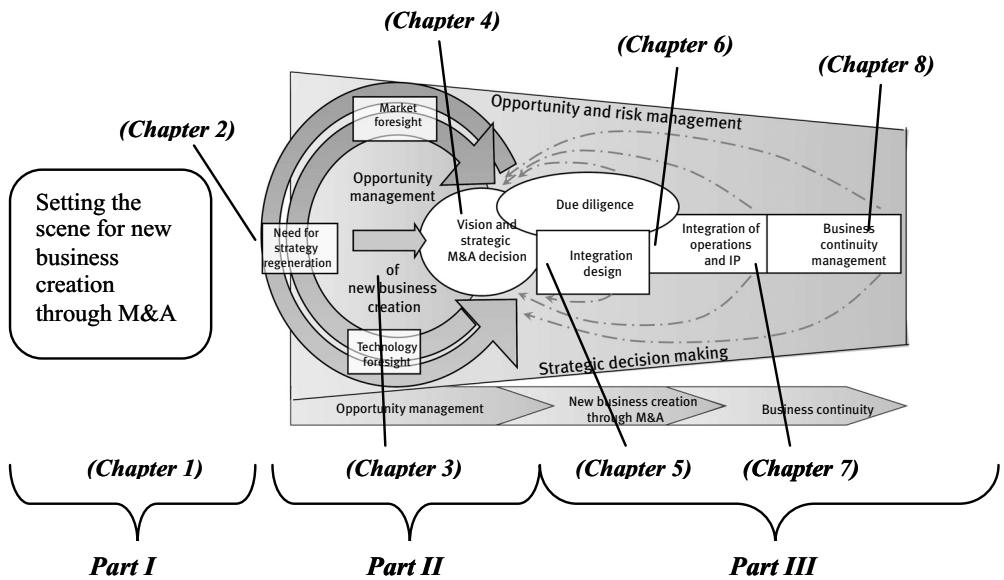


Figure 2. The structure of the book

This book is divided into three parts, of which parts two and three are the most substantial. *Part I* lays the groundwork for the phenomenon under scrutiny, NBC through M&A, introducing the topic and the focal concepts. *Part II*, which comprises Chapters 2, 3 and 4, covers the process from strategic planning to the identification and evaluation of new business opportunities. It brings in viewpoints related to strategic decision-making, opportunity identification and the risk-conscious evaluation of new opportunities. *Part III* focuses on the acquisition and integration of the new business, and on business continuity management. Chapters 5 and 6 describe the key issues related to M&A, in both the pre-acquisition and the post-acquisition phase. Chapter 7 discusses the internal and external implications, such as intra-organisational knowledge transfer and customer retention. Chapter 8 focuses on M&A success and value creation, and introduces the concept of business continuity management. Chapter 9 concludes the book in terms of summing up and discussing the more general managerial contributions and implications.