M&A MISTAKES PEOPLE MAKE: THE BUYER'S SIDE

Part 1 of a two-part series on things that make M&A go wrong

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In the next couple of blogs I will address merger and acquisition issues. This blog will address five common mistakes of buyers. A subsequent blog will likely take the same approach to the five common mistakes of sellers.

As I mentioned in previous blogs, the merger and acquisition wave is beginning to approach the shore. The consolidation will involve some community banks combining with larger institutions or each other, and some of the larger institutions continuing to consolidate their geographic base.

Over the course of my 30-plus years in this business, I have noted five common mistakes among buyers in connection with bank merger and acquisition transactions.

1. Getting the board ahead of the numbers.

When the board makes a strategic decision that it makes sense for the bank to expand geographically through acquisition, it often results in a "bias" toward acquisition. The board is all "hepped" up on doing an acquisition before the board members even see whether the numbers will work.

Keep in mind, the board's primary obligation is to enhance the value for the holding company shareholders, so if the numbers do not work on an acquisition, even assuming that execution risk and integration risk is managed, then it should not be done.

Sometimes the board simply "gets ahead of the numbers."

2. Not conducting adequate due diligence.

An obvious tenet of mergers and acquisition is due diligence of the target institution by the buyer. This due diligence has to be thorough. In a merger transaction, the buyer obtains all assets and liabilities of the target institution, both known and unknown.

It is tough enough to do due diligence on credits already on the books. It is twice as tough to anticipate unfiled lawsuits and other contingent liabilities. Due diligence needs to be thorough, complete and analyzed completely.

3. Buyer's failure to lock up key personnel of the target.

One of the most disappointing acquisitions for a buyer that I witnessed involved a large regional bank's acquisition of an approximately $500 million bank. The large regional obtained no employment contracts or non-compete agreements with the senior management team of the seller.

You guessed it-as soon as the deal was consummated, the management group figured they would do it again, which they did. When I inquired of the buyer why it did not get any non-competes or lock up the individuals, their comment was, "With as much of our stock as we were giving them, we did not think they would do anything to hurt us."

Yeah, right.

Make sure you lock up key individuals.

We kid a lot in the acquisition business about "slash and burn," firing a lot of people, etc., but the reality is, most buyers do not have excess management, so they need to lock up key individuals, both from a management standpoint and from a non-compete standpoint.

4. Buyer using the wrong method of payment.

When we consider alternative methods of payment in a bank merger and acquisition, it is either cash from the buyer, stock of the buyer, or a mixture of cash and stock. It is important to figure out what it is the seller either wants or will accept. Often, acquisition transaction currency is driven by the seller's needs and desires.

If the buyer has a listed and traded currency that could be issued without being massively dilutive, particularly to book value, to the shareholders of the buyer, then that may be the best currency to use. If the buyer's stock is trading at a very low multiple, a buyer's approach in this day and time may simply be to make what would otherwise appear to be a lowball offer that will be paid for in their stock, which may be trading in the 75% or 80% of book value range. Do not use the wrong method of payment.

5. Why buy it if you can steal it?

I remember having a discussion with a client who was considering branching into the next town, or alternatively, buying a small community bank that was in that town. As they listed the issues, the board identified the positives and negatives of acquiring this particular institution.

The positives of buying this institution were that they got its location, they got its building, they got its people, they got its loans, and they got its credit culture.

The negatives of buying this institution were that not only did they have to pay a premium, but they also they got its location, they got its building, they got its people, they got its loans, and they got its credit culture.

Why would you go buy an institution that has "issues" and contains significant execution risk if you can move in next door and take the business for basically nothing?

These certainly are not the only mistakes I have witnessed by buyers in bank acquisition transactions over my career, but they are certainly common ones.

Editor's Request: Have you seen M&A errors by buyers? Share them with fellow readers below.

About the Author

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