Bringing Brand into M&A Discussions

Misunderstanding brands can put deal value at risk

By Suzanne Hogan, Simon Glynn, and James Bell

Companies are looking farther afield for mergers and acquisitions. But it's worrying that so many deals are completed with so little discussion of the long-term impact of the merging companies' brands on shareholder value. Here are three ways to bring brand issues into the picture early on.

Mergers and acquisitions (M&A) have re-emerged globally as important paths to stronger corporate growth. What's good is that deal-making today is marked by more due diligence by both sides. What is not good is that long-term plans for the merged brands are still largely an afterthought.

There is now ample evidence to show that brand decisions made—and as importantly, decisions avoided—can affect an organization's long-term ability to achieve its strategic objectives. That is especially true in the case of mergers and acquisitions. If an acquirer's top managers give too little attention to brand or fail to understand each brand's strategic role, they may overpay for assets that are not used. They may also unwittingly put constraints on future business strategy or build high barriers to effective integration of the two companies.

The tale of Volkswagen's 1998 acquisition of Rolls-Royce Motors illustrates how brand plays an important role in M&A activities. VW spent £430 million to buy the Rolls-Royce company but the deal didn't include the illustrious Rolls-Royce brand. (A history of company splits, brand cross-licensing, and legal trigger clauses meant that Rolls-Royce effectively had to sell the brand separately.) When rival BMW then acquired the rights to the Rolls brand and its visual icons for £40 million, critics believed that VW had lost out. They appeared to be proved right as BMW revitalized the Rolls-Royce marque starting from only a name and a radiator grille.

Bentley Bolt from the Blue

But there was much more to the story than that. VW had seen hidden value in the business that it purchased. The Rolls-Royce Motors company included the Bentley brand—lustrous in its own right. VW set about transferring some of the Rolls-Royce brand equity to Bentley. In 1998, the year of the deal, Rolls-Royce Motors sold 1,600 high-end cars—a mix of Rolls and Bentleys. Five years later, when BMW sold 800 Rolls-Royces, VW sold 700 traditional Bentleys—along with more than 6,000 of its racy new Bentley Continental GT.

In short, VW has deftly used its new, higher-volume Continental GT not only to grow Bentley revenues but also to create the visibility that Bentley needs to be an aspirational luxury car brand.

There's a similar story in the travel agency business. When Vivendi Universal sold Havas Voyages in 2000, the Havas name—known across France for decades—was not part of the sale to German travel company C&N because C&N's plans called for rebranding as Thomas Cook AG—another renowned name in travel. But French travel company TUI saw plenty of brand equity in the Havas name; a recent survey showed that Havas Voyages was the fourth most recognized tourism

Suzanne Hogan is a New York-based senior partner, Simon Glynn is a London-based senior partner, and James Bell is a New York-based senior partner of Lippincott Mercer. They can be reached at suzanne.hogan@lm.mmc.com, simon.glynn@lm.mmc.com, and james.bell@lm.mmc.com.

brand in France. In March 2005, French travel firm TUI bought the rights to the name from Vivendi and hopes to open 150 Havas branches across France in the next few years.

The central lesson of the Bentley and Havas stories points to the importance of assessing overall brand value for the merged organization long after the deal is complete. What matters is a dynamic, forward-looking stance on brand value, not a static picture based on historic brand asset valuations (see Exhibit 1). This calls for an approach to valuing, negotiating, and managing brands during a merger that:

- Determines how the brands shift demand in practice
- Connects to the business strategy and overall brand strategy
- Supports, and is supported by, the post-merger integration plan

New Importance for Brand Considerations

According to Mergerstat, 2004 was "a year to remember" for transactions; for the first half of 2005, the research firm reported that deal values were climbing significantly on both sides of the Atlantic. Observers were predicting the biggest year for deal-making in Europe since 1999-2000.

New and assertive acquirers have appeared on the global stage, fueling fresh growth opportunities. China's Lenovo bought IBM's PC operations, for example, and Indian steelmaker LN Mittal last year bought U.S.-based International Steel Group. French liquor company Pernod Ricard purchased Allied Domecq, and Holland's VNU is acquiring U.S. healthcare provider IMS Health.

Deal-making momentum likely won't slacken any time soon. Private equity firms are sitting on huge backlogs of investment capital. And growth-minded executives, backed by ample cash, solid stock valuations, and greater lending liquidity from the banks, are now up-ending M&A markets that have been the province of the private-equity buyers for years.

Yet mergers and acquisitions continue to concern and confound many experienced senior managers. You don't have to look far to see the outcomes in the poor performance of some of the major M&A deals of the late 1990s. Studies show that 70% of major acquisitions fail to deliver real long-term value for shareholders.

"Too Caught Up" in the Bidding Process

When a merger is under way, the demands of

Exhibit 1 **Status report on brand activity in M&A deals**

The missing link in M&A deals	Recognition of the role of brand in the business logic of the deal and in the post-deal implementation—currently hidden by backward-looking asset valuation of brands
Why it matters	• Risk of overpaying for assets not used • Increased post-merger implementation risks • Opportunity cost of "free" awareness-building at time of announcement
What to do ahead of the deal	Future-looking assessment (vs. backward-looking asset valuation) of how brand will contribute to the merged business • Based on how the brands shift demand in practice • Linked to the deal strategy • Linked to overall brand strategy • Part of the transition process from day one

negotiations and the pressure to close the deal often create a short-term focus and shortsighted actions. It becomes difficult to stay focused on how value will be created long after the deal is completed. One recent survey notes that more than a third of executives who have done major mergers or acquisitions now acknowledge that they got “too caught up” in the bidding process to do truly effective due diligence.

While managers today are generally more aware of the asset value of brands in general than they were a decade ago, they tend to think of brands largely in static, passive terms. They’re less aware that brands can actively alter demand patterns, and they often don’t see that a brand’s value is more volatile than most other assets.

A brand’s value is not fixed in isolation; it is as much a consequence of the merger or acquisition and the subsequent business strategy of the merged entity as it is an input to them. That’s why the risk extends beyond just ignoring a brand’s value; the potentially bigger risk is valuing a brand in a way that has no relation to how you plan to use it in the new business. The result could be a big future write-down or an equally big constraint on the future business strategy.

Some companies have mastered the skills necessary to take an active, forward-looking approach. They have been able to convincingly answer key questions about brand before any deal talks heat up, and they have drafted the necessary steps to manage their brands and those of their acquirees right through the M&A transaction. (See sidebar on page 38, “The Brand-Builder’s M&A Checklist.”) Our analysis of their tactics yields these three guidelines:

1. *Gauge value by how the brands will affect demand.*

Many senior managers of target companies come to the bargaining table with impressive facts and figures on the value of their brands. But the acquirers owe it to their companies and shareholders to do their own research. Otherwise, they risk overpaying for assets that may have lost their luster or that may not translate to the business environment facing the newly merged company.

For all of the mystique about brands, companies should value them for only one reason: their ability to shift demand. (Usually that implies demand from customers, but it can also mean demand from employees, investors, and others.) Understanding how a brand shifts customer demand—and how it will do so long after the deal is done—is what matters. Using only a balance-sheet method for determining value provides little guidance on some of the more subtle predictors of how brands alter demand—and therefore current and future brand value.

The due diligence has to go much further than the figures available in the target’s finance department. It’s crucial to conduct detailed primary research on customers and markets, seeking answers to questions such as:

- Do customers have a preference for the brand in the marketplace?
- How much of a premium do they pay for it? How is that premium changing?
- How would their buying behavior change without the brand in the marketplace?
- How much of the apparent brand value is actually driven by product features or distribution channels that are associated with the brand?
- What are the benefits or risks to the brand or to the company if the brand were to be dropped? Could its equity be transferred to another brand and if so, how quickly?

Answering these questions requires a different set of research and analysis than a balance-sheet-based valuation.

When cable-services provider Comcast acquired AT&T Broadband in 2002, Comcast had the option to license use of the venerable AT&T brand due to its presumed equity in the marketplace. However, by the time of the deal, the AT&T brand was beginning to lose its reputation in broadband services. So Comcast’s management team made a decision based on its own long-term brand

The Brand-Builder's M&A Checklist

There are distinct points at which brand assessments should be made both before and after a merger. Specifically, there are crucial brand audit and valuation steps that help determine the brand strategy and architecture for the merged entity—steps that inform the "intent to merge" announcement. It is also important to plan the brand transition strategy and earmark the necessary resources and budgets before the deal is declared complete. Afterward, the actual launch or relaunch of a brand calls for detailed design and implementation activities, followed by continued evaluation and monitoring of the success of the new brand. The project flow shown here describes development of a new brand following a merger or acquisition, but the key points about "before" and "after" initiatives hold true for any brand assessments made during an M&A transaction. ❖

Exhibit **Status report on brand activity in M&A deals**

1. Pre-deal phase

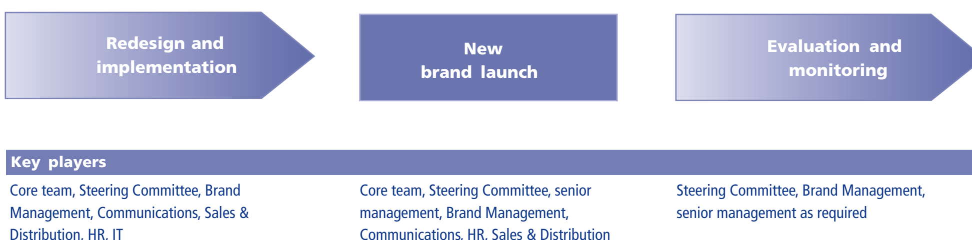
The pre-deal phase is driven by senior and strategic management for both parties and determines the brand strategy and architecture for the merged entity.

2. Brand transition

Significant brand transition planning involving most functional areas should occur prior to deal close.

3. Post-deal phase

In the post-deal phase, a number of activities should be carefully coordinated to ensure successful implementation and brand rollout. Most functional areas of the organization need to be involved.



strategy of building the Comcast brand. Their stance: Why confuse the marketplace? AT&T's broadband business became Comcast; well-planned communications programs helped ease the transition for customers and employees alike.

The lesson is that it's critical to conduct your own research and to conduct the right kind—more than just a static dollar value and simple assessments of image and awareness. What's needed is to determine the brand's value in driving business outcomes.

2. Tie the brand strategy firmly to the business strategy.

Mergers and acquisitions have a strategic business purpose. It may be to achieve operational synergies, to broaden a range of products or services, to gain a new geographic presence, reach a new customer segment, or expand share of wallet with an existing segment. There's trouble ahead if the business purpose collides with an immutable brand strategy.

The collision can quickly become apparent at the product level. Resistance can be fierce and territorial if management intends to consolidate product brands after a merger. Then it is incumbent upon senior executives to clearly communicate the broader strategic purpose of the deal—and to amend incentives accordingly. By communicating a vision for the entire brand portfolio—expressing the issue in terms of how brands will shift demand—U.S. executives in particular can help to balance opposing views that say that brands are assets that can't be written off. (U.S. accounting standards recognize the value of intangible assets.)

The corporate brands and the products' brands may or may not be important to the deal. Executives need to honestly evaluate the "brand factor" well in advance of the day that the deal is signed. If your long-term strategy is to migrate to a single brand, it is best to determine the acquired brand's reasonable value to the company over time. Otherwise, the lack of pre-planning can hurt shareholder value.

We recently worked on one program where a company's brand model (and related strategy) indicated that it should subsume the acquired brand under the parent name. But somehow that fact was lost in the shuffle at the time of the deal, and a $350 million value was assigned to the brand in perpetuity. That value will have to be written off if the company's acquisition is ever to align with the desired brand strategy and the true value for which it was purchased—the capabilities, not the brand name.

In short, the brand model and brand strategy must be considered in any merger. Otherwise, companies may miss the opportunity to be known and valued for their full range of services.

We know of another major corporation that expanded its services by acquiring several companies in another industry sector. But the company continued to be known only for its original offerings; none of the capabilities of the acquirees changed how customers and prospects viewed the company's brand because the new subsidiaries were allowed to retain their brand names. That would not have mattered if the strategic purpose of the acquisitions was simply to acquire the new capabilities. But the company had sought to broaden its customers' perceptions of its brand as well.

3. Develop and manage the brand transition plan.

An immediate transition to a new brand can accelerate and energize the transition process. Internally, staff can more quickly feel part of the new combined group, and will more naturally challenge their past ways of doing things, questioning what must be different under the new brand. Externally, immediate adoption of the new brand allows merged companies to capitalize on the free publicity surrounding an acquisition or merger announcement.

That's particularly true when well-known names are subsumed under a new brand name. In the U.K., two long-familiar consumer-services companies were replaced by a fresh, invented name. But the new corporate name

came a few years after the deal had been done. The company had missed a valuable publicity opportunity at the time of the merger; by the time the new name appeared, there were few cost-efficient ways of building equity in it.

Some years back, IBM had skillfully managed conflicting brand issues during and after its acquisition of software provider Lotus Development. At first, Big Blue—whose master-brand approach had been sacrosanct—left the Lotus brand alone, both as a corporate entity and as a product. The IBM name appeared in small print but the Lotus brand dominated. Over time, though, IBM brand managers "migrated" Lotus to a product brand. They had continually monitored the market's perceptions of the IBM and Lotus brands to determine the right time to make the switch.

Why did IBM bend its rules? One reason was to retain key talent; the Lotus culture was a world away from that of IBM, and IBM feared that a heavy-handed approach would quickly cause key employees to quit. Another reason was that the IBM and Lotus images were in conflict. At that time, IBM was known as a hardware company while Lotus was clearly a software firm. So to communicate independence, retain talent and customers, and avoid the image conflict, the decision was to tap the equity in the Lotus brand until the time was right to subsume it under IBM's brand.

A well-managed brand transition plan can provide a fine blueprint for a global growth strategy, as ABN AMRO found out. At the end of the 1990s, the Dutch financial-services giant was a household name in Holland but little known elsewhere. It's core challenge: to take a Northern European regional brand and make it into a recognized global powerhouse—crucial to its success as it set out to expand by acquisition.

In 1998, ABN AMRO acquired Banco Real, Brazil's fourth-largest private-sector bank. We helped the Dutch executives study the comparative value of Banco Real's brand equity, devise positioning platforms, and decide what would preserve Banco Real's brand leverage while firmly planting ABN AMRO's identity in Brazil. Their decision: to keep the Banco Real name everywhere but to apply the parent's green and yellow identity scheme and to endorse it with the ABN AMRO name in small letters.

The Dutch company has since applied versions of its successful Banco Real solution to a series of acquisitions. Previously, its approach had been to allow new subsidiaries to act independently and retain their identities. Although there was a clear ABN AMRO parent identity, there was no enforced policy for how the new units should or shouldn't be folded into the ABN system—organizationally or in terms of brand. But with more services on offer, more segments, more marketing programs, and more media options than ever, the bank risked letting inconsistency dilute and eventually erode its corporate brand. Following a corporate reorganization in 2000, ABN AMRO's leaders devised a company-wide strategy that introduced disciplined processes for how new subsidiaries adopted the ABN AMRO brand.

Brand Decisions, Early and Often

Businesses are looking further afield—increasingly around the world—for potential acquisitions that can help them drive top- and bottom-line growth. But there are worrying indicators that brand issues are not being properly built into the due-diligence processes that precede detailed negotiations or into the integration activities that follow a merger.

Business leaders can no longer view brand management during a merger or acquisition simply as something for the marketing staff to sort out after the deal is done. Timely attention, focusing on how brands shift demand, is essential to validate and shape the deal, and to guide customers and employees smoothly through the transition. Ideally, acquirers should have detailed brand decision systems in place before they draw up their search lists. The decision systems should include robust research methodologies for determining both brand value and

the true drivers of brand equity.

At the very least, acquirers must establish what they are buying and why. They have to push brand valuations beyond assumed dollar values and well beyond simple assessments of image and awareness. It is crucial to determine the target brands' value in driving long-term business outcomes. Anything less will fail to spur growth worldwide and will eventually shortchange shareholders. ❖