

Catching a Second Wave: Capturing Unrealized Value from Past M&A

Cost synergies and performance improvement opportunities often are not fully realized during initial post-merger integration (or PMI) efforts. Many of our clients therefore have initiated “second wave” efforts, 2-5 years after a merger or acquisition has closed, to unlock these additional synergies or benefits. In some cases, we have seen companies wait 10+ years to capture the full value from prior M&A deals. These efforts, typically communicated as productivity or operational effectiveness programs (and never as an integration exercise), can reduce costs by up to 20 percent in the areas examined.

The current economic climate dictates that now is a good time to revisit earlier mergers and acquisitions:

- Little M&A activity is occurring now, so your business development staff can conduct a post-integration review or “audit” to assess whether intended synergies and value from prior M&A have been fully realized. During such a review, current operational approaches and already realized synergies are compared to the plans that were established during the earlier deals’ due diligence and synergy study processes.

- Earnings and cost pressures provide an incentive to review prior post-merger integration results and the motivation for the senior management team to address the “tough” decisions that may have been bypassed before and develop plans to capture the untapped value.

Determining whether the originally intended synergies and value have been already harvested or are still available is a first step toward capturing unrealized synergies and contributing value and earnings later this year and certainly in 2010.

The value to be unlocked from “old deals”

Since most utilities’ merger and acquisition activity are “old deals” (having occurred at least 2-3 years ago), many companies can take advantage of two primary sources of “second wave” synergies and benefits:

- **Reduction in internal and external barriers to full integration:** External and internal resistance and constraints (e.g., cultural, political, regulatory) often make it difficult to fully integrate and capture synergy savings when the deal is new. After some time has passed and initial integration efforts, oversight, and scrutiny have subsided, management often can more effectively address these barriers, more fully integrate the companies, and capture more synergy savings. For example:
 - Consolidating support staff and back office functions
 - Consolidating or closing facilities (selling property or buying out leases)

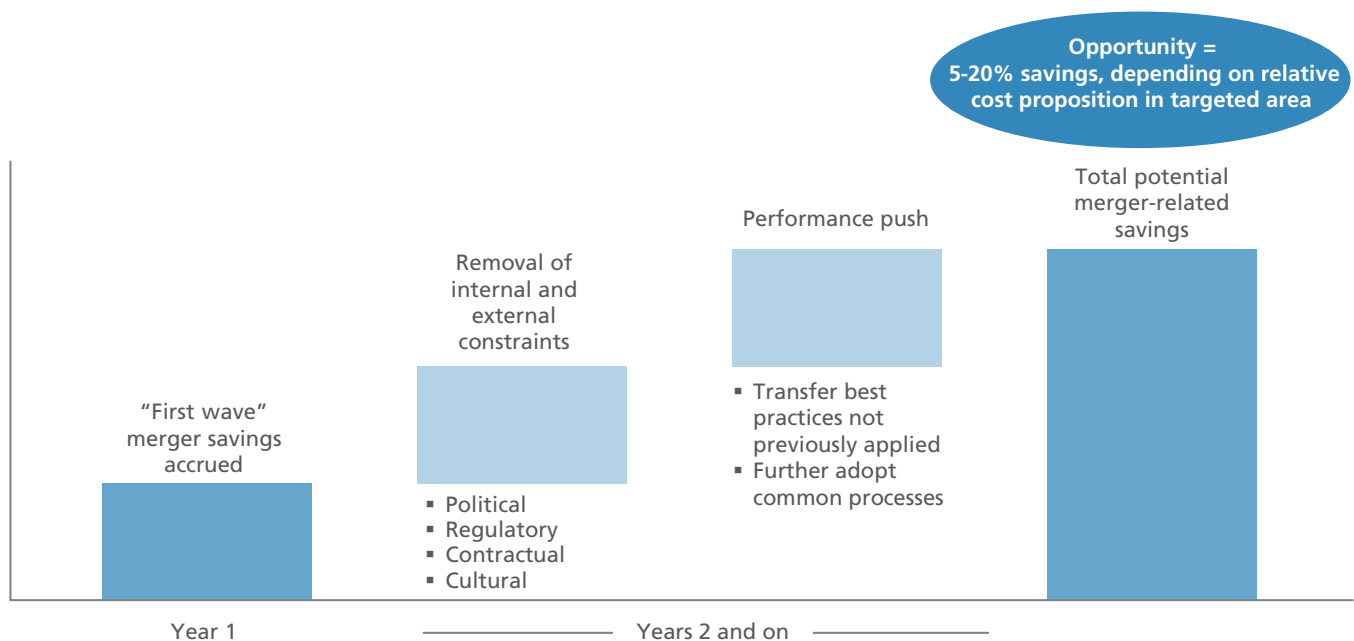
- Streamlining organization structures, and eliminating any “extra” positions created to “find homes for individuals” at the time of initial integration

- **Increased knowledge of the partner companies:**

New savings and improvement opportunities typically also surface as executives increase their knowledge of one another’s predecessor companies. These latter opportunities can give a utility a “performance push.” For example:

- Discovering exceptionally well performing areas/practices to transplant into other operating entities or organizational units
- Uncovering areas where prior poor performance had been hidden
- Gaining greater appreciation for the strengths and weaknesses of managers and realigning the management team

Exhibit 1 “Second Wave” Savings Opportunities



Conducting a second wave review or “audit”

A second wave integration review or “audit” can help refocus utilities on realizing or exceeding the synergies that the merger was intended to produce in the first place. Because so much changes in the first year or two after a merger or acquisition closes, managers can lose sight of both the cost savings they need to realize from the merger and the opportunity that the merger gives to reposition the combined business to achieve shareholder value growth.

Oliver Wyman has recently worked with several utilities that recently “celebrated” the second, fifth, and eighth anniversaries of major acquisitions or mergers. In each case, the passage of time and decreased external scrutiny, as well as ongoing cost and earnings pressures, created an environment in which executives were increasingly receptive to second wave opportunities, such as:

- Consolidating back office, transactional operations into a single location

- Combining call centers, rather than keeping separate centers for each operating company
- Closing facilities, including the headquarters offices of an operating company, to more efficiently locate staff in one building
- Streamlining the management structure by reducing the number of officers, in order to leverage the “best” managers, speed decision-making processes, and lower cost
- Driving the adoption of best practices and “enforcing” the use of common practices, processes, and standards across the entire organization

Given today’s economic realities and the likelihood that other options have been already exhausted, now is the time to understand whether unrealized synergies from earlier deals are still available and determine how that value can best be realized.

Exhibit 2 Representative “Second Wave” Savings Sources

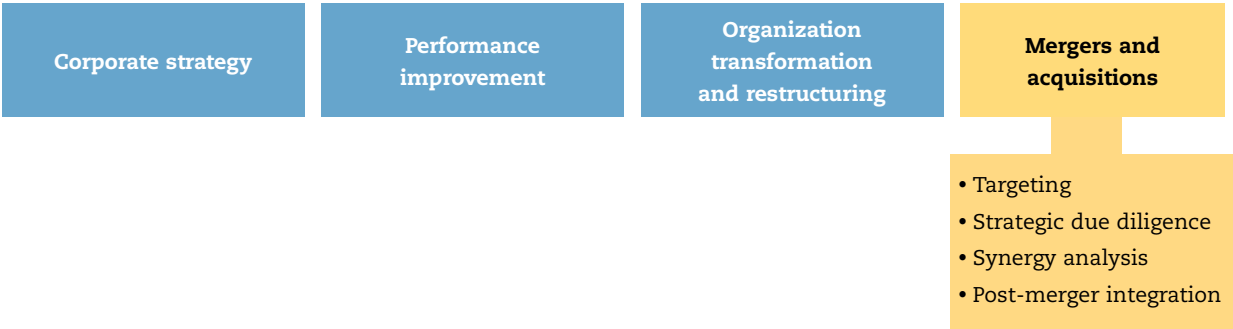
Post-merger event	Potential savings categories				
	Personnel	Supply chain	Facilities	IT	A&G overhead
Political and regulatory pressure reduced or eliminated	✓ Consolidate HQ and back office functions Consolidate call centers		✓ Close or consolidate buildings (corporate, customer service)		
Contracts and leases expire		✓ Optimize procurement and vendor management Optimize size and mix of fleet	✓ Close or consolidate buildings (e.g., field service centers)	✓ Eliminate duplicative licenses	
Best practices and well performing geographies emerge	✓ Improve productivity Streamline processes	✓ Adopt best material and construction standards		✓ Adopt best operational systems	✓ Re-examine services provided (and their value)
High- or poor-performing managers emerge	✓	✓	✓	✓	✓

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