

ADVANCES IN MERGERS
AND ACQUISITIONS

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ADVANCES IN MERGERS AND
ACQUISITIONS VOLUME 18

**ADVANCES IN MERGERS AND
ACQUISITIONS**

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INVESTOR IN PEOPLE

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a marvel – a jargon-free business book based on serious research that offers genuine insights with clarity and sometimes even wit ... It should be required reading not just for executives but for investors as well.

His latest bestselling book is *SUPERBOSSSES: How Exceptional Leaders Master the Flow of Talent*, which was named one of Amazon's "Best Books" on business and leadership for 2016. LinkedIn Chairman Reid Hoffman calls it "a leadership guide for the Networked Age." Professor Finkelstein is a Fellow of the

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INTRODUCTION

Cary L. Cooper and Sydney Finkelstein

The *Advances in Mergers and Acquisitions* is a scholarly collection of reviews of research, theories and case studies of mergers and acquisitions (M&As) in a variety of contexts and countries. This volume is the 18th in this annual series exploring the following issues: why the success rate of M&As is still not very good, how Boards influence M&A activity, what the roles of M&A advisors are in the process, the role of diversity in the context of M&As, stakeholder relationships in the context of M&As, why research has not focussed on family businesses in the M&A field as much as it should, making M&As less risky as a strategic investment, merging cities, pre-merger and acquisition strategies and finally, how ‘value’ has been used or not used in M&As.

Mitchell Lee Marks explores why after 30 years of M&A research the success rate of M&As is still very low, and how human factors tend to contribute to their success or failure. Mike W. Peng and Joyce C. Wang explore how network ties formed by directors may shape M&A processes and outcomes. Janice M. Gordon, Gonzalo Molina-Sieiro, Kimberly M. Ellis and Bruce T. Lamont ask the question ‘are M&A advisors padding their pockets or a source of expertise’, basically what is the role of M&A advisors in this complex process. Annette Risberg and Sofie Skovbo Gottlieb explore the literature on women and minorities in the context of M&As, how and to what extent are diversity and gender issues studied in merger research. Simon Segal, James Guthrie and John Dumay assess the significance of stakeholder relationships in an Australian mega-merger case study. It highlights how M&A events relate to stakeholder behaviour. Olimpia Meglio and David R. King highlight the paucity of research on family businesses in the context of M&As, and how M&As ‘are primarily regarded as a tool to solve succession problems’. Fadi Alkaraan explores the influence of due diligence processes on strategic investment decision making in an effort to make M&As less risky. Janne Tienari, Kari Jalonen and Virpi Sorsa highlight now that little research has been done on city and municipality mergers, which are so important to the economy of individual countries, and how this research could shed light on organisational M&As. And finally, Sally Riad and Urs Daellenbach examine the concept of ‘value’ and its utility in M&A research, and in understanding the M&A process.

The research outlined in this volume, and all the past *Advances* books, is an important body of scholarship that should help minimise the negative consequences of M&As in the future, whether in personal, organisational or financial outcomes – and highlight good practice going forward, as businesses look for

growth and value creation. We hope you will find this a useful addition to the M&A literature in an effort to improve the success rate of these ventures.

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CHAPTER 1

A RESEARCH AGENDA TO INCREASE MERGER AND ACQUISITION SUCCESS

Mitchell Lee Marks

ABSTRACT

Scholars have been conducting serious research on the human, organizational, and cultural aspects of mergers and acquisitions (M&A) for 30 years. Yet, over this period, there have only been modest improvements in the M&A success rate. In this chapter, the author examines corporate combinations, describes how human factors contribute to their failure or success, and identifies key research questions whose answers can help to improve the M&A success rate in both financial and human terms. The author proposes research questions for the key phases of a deal, including buying a company and putting companies together. And, reflecting an emerging trend among some frequent acquirers to build an internal competence in M&A execution, the author also proposes research questions for how to accelerate the process of learning from past combinations to better manage future ones.

Keywords: Merger; acquisition; integration; culture clash; transition teams; cross-border

INTRODUCTION

Many motives prompt executives to acquire or merge with another organization.¹ In some cases, a combination helps a firm move quickly into a new market or

product space or pursue a strategy that would otherwise be too costly, risky, or technologically advanced to achieve on its own. Other times, deals are opportunistic, such as when a troubled competitor seeks a savior or when a bidding war ensues after a firm is “put into play.” Still other times, acquisitions or mergers can be defensive moves to protect market share in a declining or consolidating industry. The overarching reason for combining with another organization is that the union will enable a firm to attain strategic goals more quickly and inexpensively than acting on its own (Haspeslagh & Jamison, 1991).

Despite their popularity, most mergers and acquisitions (M&A) are financial failures and produce undesirable consequences for the people and companies involved. While target-firm shareholders generally enjoy positive short-term returns, investors in bidding firms frequently experience share price underperformance in the months following acquisition, with negligible long-term gains (Agrawal & Jaffe, 2000). In addition, M&A can exact a heavy toll on employees (DeMeuse & Marks, 2003; Mische, 2001). A longitudinal study of 10,000 US employees representing 4,000 organizations found those from organizations that had been engaged in M&A reported significantly less favorable results than those who had not been involved. This held true for every industry group and every facet of working life measured (Wiley & Moechnig, 2005).

Many factors account for the dismal M&A track record, including paying the wrong price, buying the wrong company, or making the deal at the wrong time. My own 30-year research program with Philip H. Mirvis finds that the *processes* used to put companies together are integral to a deal’s success versus failure (Marks & Mirvis, 2010). This encompasses the formation and operations of the buying team (Mirvis & Marks, 1992), how the firms are integrated (Marks & Mirvis, 2000), and learning from current deals to better manage future ones (Marks & Mirvis, 2001). In the rest of this chapter, I suggest research opportunities to assess and understand processes in each of these three phases of a deal.

BUYING A COMPANY

Buying a company encompasses strategizing, scouting, assessing and selecting a partner, deal making, and preparing for the eventual combination. The typical approach involves a “tunnel vision” on the financial aspects of the deal. Buyers concentrate on what a target is worth, what price premium, if any, to pay, and how to structure the transaction. The successful approach, by comparison, also emphasizes finance but adds careful attention to how a combination advances the business strategy of a firm, due diligence on behavioral and culture factors that might complicate the combination, and a clear picture of how the firms will be integrated.

Research Questions on Buying a Business

A review of relevant literature as well as practical experience suggests some key areas for future M&A research on the workings of buy teams.

M&A Motives

To what extent are M&A “buy” decisions motivated by strategic intent (e.g., market power, efficiency, asset redeployment, and market discipline) versus manager’s self-interest (e.g., hubris, empire building, survival, and personal financial gains)? This question applies to the overall make-versus-buy decision, the selection of a partner, and the price paid. Obviously, corporate pronouncements and executive talking points express the business case behind any deal. Yet a blue-ribbon panel of financial experts concluded that chief executive officer (CEO) ego was the primary force driving M&A in the United States (Boucher, 1980). Another study found that the bigger the ego of the acquiring company’s CEO the higher the premium a company is likely to pay for a target (Sirower, 1997).

If the true motives behind a combination have more to do with “nonstrategic” forces – say, the desire to run the largest company in an industry or fear of being swallowed up by competitors – then value creation is unlikely because there are few benefits to be leveraged by joining forces. To get at these factors, researchers might look into the pattern of purchases by regular acquirers and to what extent it builds out a clear and coherent business strategy. Those with a clinical mindset might, as Harry Levinson (1976) has done, explore the mindsets of buying CEOs and how their ambitions and fears factor into their M&A proclivities. They might also investigate instructions given to buy teams, pressures on them to do a particular deal, and considerations given to alternative courses of action.

Research question 1a. To what extent do strategic versus non-strategic motives drive M&A buy teams and what is the relationship between those motives and the price paid, partner selected, and synergies achieved by a deal?

Behavioral and Cultural Due Diligence

When due diligence focuses exclusively on the financial makeup of potential M&A partners, analysts overestimate revenue gains and cost savings and underestimate the resource requirements and headaches involved in integrating businesses (Lodorfo & Boateng, 2006). Adding in behavioral due diligence – the process of investigating a potential partner’s talent, organizational makeup and culture – enables a buyer to understand if the values of the potential partners are compatible, if the bench strength exists to replace managers who might depart, if all parties are on the same wavelength regarding synergies and what it takes to combine, and if there is enough trust and chemistry to propel the combined operation into becoming more than the sum of its parts (Carlton & Linebury, 2004; Gebhardt, 2003). Behavioral due diligence pays off: one study found that successful acquirers were 40% more likely to conduct thorough human and cultural due diligence than unsuccessful buyers (Anslinger & Copeland, 1996).

Research question 1b. How do buy teams consider behavioral versus financial due diligence in their analysis and to what extent does behavioral due diligence yield better M&A decisions?

Buy Team Make Up

Most members of traditional due diligence teams come from financial positions or backgrounds. They bring a financial mind-set to the study of a partner, and their judgments about synergies are informed by financial models and ratios. They do not necessarily bring an experienced eye to assessing a partner's "fit" in areas of engineering, manufacturing, or marketing. As a result, there is a tendency for "hard" criteria to drive out "soft" matters: if the numbers look good, any doubts about organizational or cultural differences tend to be scoffed at and dismissed.

Mirvis and I have argued that the traditional membership of due diligence teams (e.g., financial analysts and strategists) be augmented by people from technical, operational, and HR functions. More research is needed to understand how this diversity in interests and expertise influences M&A analysis and team dynamics.

Research question 1c. To what extent does functional and operational diversity in due diligence team membership contribute to better M&A decision making?

Buy Team Decision Making

M&A underperformance is sometimes attributed to the "rush to close" the deal at the expense of attending to factors that could help or hurt its eventual success (Ashkenas & Francis, 2000). Why would companies buy something when their buy team has not thoroughly "looked under the hood?" Several scholars have documented how decision making traps – anchoring in initial perceptions, escalating commitments, and cognitive overload – can lead buyers to follow faulty assumptions and multiple misjudgments (Duhaime & Schwenk, 1985). Thus Mirvis and I have also proposed that buy teams be schooled in decision-making biases and apply decision-making tools and interventions to their deliberations. What are needed are studies of how these practices, studied in the lab, can operate in the field.

Research question 1d. What decision tools and interventions improve an M&A buy team's analyses and decisions?

Combination Forms

Organizations can link together in many forms of legal combinations, ranging from a relatively informal network to outright absorption of one entity by another. The forms of combination vary by the depth of commitment and level of investment between the organizations joining forces. A *strategic alliance* is a cooperative effort by two or more entities in pursuit of their own strategic objectives. A *joint venture* (JV) goes further, by establishing a complete and separate formal organization with its own structure, governance, workforce, procedures, policies, and culture – while the predecessor companies still exist. A *merger* usually involves the full combination of two previously separate organizations into a third (new) entity. An *acquisition* typically is the purchase of one organization for incorporation into the parent firm.

Important differences distinguish these forms. As financial investment and risk increase, so does the control held by the lead company. Along this same line, the impact on the target company or lesser partner grows, as do the requirements for integration. If, for whatever reason, a combination does not live up to expectations (or if the needs of either party change), then the formal bonds of a merger or acquisition are much more difficult to undo than are the relatively time-bound and looser ties of an alliance or JV.

Research question 1e. To what way does the form of a combination influence its eventual strategic, financial and human outcomes?

PUTTING COMPANIES TOGETHER

After the deal receives legal clearance, the real work of integrating companies commences. Three aspects of M&A practice at this point beg research attention. First is the tendency for companies to fail to fully take account of the “human side” of M&A. Senior executives, once named to top posts, can’t relate to the uncertainty and insecurity experienced by employees down the line. Middle managers get caught up in their own anxiety and fail to communicate with their people. Meanwhile, HR departments are busy fire-fighting rather than moving the combination forward.

Second is the increasingly common practice of forming integration planning teams with membership from both sides of a deal. Too often, however, these teams are ill-equipped to work together. They frequently are marred by conflict, engage in horse-trading, or simply settle for low-common-denominator decisions.

Third, the clash of cultures tends to be downplayed or ignored. A survey of European managers involved in acquisitions and alliances found that technical issues were less instrumental in producing conflicts in work relationships than differences between corporate and national cultures (Marks & Mirvis, 2010). A majority also reported that senior executives did not initially regard such differences as important.

Research Questions on Combining Businesses

Thirty years ago, we identified the symptoms of the “Merger Syndrome” as a prime cause of the individual, organizational, and culture problems in M&A (Marks & Mirvis, 1985). The Merger Syndrome is a fusion of uncertainty and the likelihood of change, both favorable and unfavorable, that produces stress and ultimately affects perceptions and judgments, interpersonal relationships, and the dynamics of the combination itself. At the organizational level, the Syndrome is manifested by increased centralization and lessened communication, leaving people in the dark about the combination and fueling rumors and insecurities. This often produces worst-case-scenario thinking that distracts employees from regular duties. All of these hamper integration, reduce productivity, and contribute to turnover of key people.

In response to these combination challenges, scholars have identified a range of interventions to counter adverse emotional reactions at the individual level (cf., [Seo & Hill, 2005](#)), improve integration planning effectiveness at the group level (e.g., [Bradley, 2003](#)), and ease the clash of cultures ([Chatman & Cha, 2003](#)).

Psychological Preparation

One way to mollify the effects of the Merger Syndrome is a “realistic merger preview” that provides detailed information regarding the timeline of a combination, how it will affect employees, and other pertinent information. In a quasi-experimental study, researchers found that employees given a realistic preview of their merge rebounded more quickly from the negative effect in areas including job attitudes, trust toward the company, and job performance ([Schweiger & DeNisi, 1991](#)).

Other interventions include educating people through readings, presentations, or discussions of human factors in a combination. A more dynamic way is through merger sensitization workshops, role plays, and other experiential activities that help people develop a true feeling of what it is like to acquire or be acquired ([Marks, 2003](#)).

Research question 2a. What kinds of interventions best prepare people to cope with the stresses of a combination?

Combination Mindsets

Combination partners typically enter a deal with distinct mind-sets. In an acquisition, the buyer and seller usually have very different psychological perspectives on the deal. The victor-versus-vanquished outlook is also found in many mergers where one of the parties is clearly seen as the lead company. Psychological mind-sets certainly influence early dealings and can dominate the critical months of transition planning and implementation. They often carry over into the combined organization.

To the victor go the spoils. Certainly, bidding wars and hostile takeovers are exhilarating for the winners. But even in a friendly deal, there are few moments in an executive’s career that equal the intensity and satisfaction of buying another company. Acquiring another organization, or assuming the role of lead party in a merger or alliance, translates into a strong air of superiority. In contrast, being acquired often is debilitating to an organization and its people. From the start, in the case of a hostile deal or one imposed by the Board, there is a sense of violation: I have interviewed executives who liken it to rape and describe their buyer as an attacker or barbarian. Even in friendly deals, acquired managers often describe themselves as being “seduced” by promises that changes will be minimal, or as being “taken advantage of” once they are forced to accommodate the new owner’s demands.

Alternatively, there are mergers which look, from the get-go, to be combinations of equals, acquisitions where a smaller business is delighted to be part of a larger company, and alliances and JVs in which both sides equally invest.

Preconditions for this *partnering mindset* include trustworthy dealings, common interests, complementary skills, and a spirit of cooperative competitiveness.

Research question 2b. How enduring is impact of the adoption and expression of winner/loser mindsets on eventual integration planning and implementation and what steps can be taken to build partnering mindsets?

Adapting to Change

Concurrent with the development of insight into the range of human reactions to M&A has been the study of behavioral interventions to address their consequences (Jian, 2007). Many aim to help people to “let go” of past affiliations and practices and move toward the new behaviors and identifications (Bridges, 1991). But some address the socio-emotional aspects of adaptation. Mirvis and I have, for example, studied “grieving meetings” where people can mourn their losses and “bury” past associations. Others favor more cognitive approaches that have people, for instance, calculate the “plusses-and-minuses” of change. Still others emphasize acculturative interventions that bring people together quickly with counterparts from the other side. Finally, there are work-based interventions that stress the behavioral role of leaders and work groups in providing psychological support.

Research question 2c. What kinds of interventions – emotional, cognitive, acculturative, behavioral – help people to adapt to changes wrought by M&A? Is there a critical period in which interventions are more versus less effective in helping people prepare for and cope with the Merger Syndrome?

Transition Teaming

Like any other start-up group, transition teams go through stages of development before they get down to performing effectively. What complicates this is that these teams are populated by representatives from each company that have their own accustomed ways of analyzing issues, sorting options, and arriving at decisions. Furthermore, they have their own and their organization’s interests to protect. This is a setup for conflict (Mirvis, 1985). Undoubtedly, criteria used in team member selection, decisions about team leadership (e.g., single or dual-leaders and the person likely to head the function or an impartial figure) and about team composition (e.g., equal representation from both sides and commensurate levels of skill and tenure) influence team dynamics.

Research question 2d. What factors in transition team member selection, team composition and leadership, and team operations promote more or less effective team decisions?

Here, too, there have been interventions proposed to facilitate transition teaming that include team building exercises, third party process facilitation, and training in conflict resolution.

Research question 2e. What kinds of interventions work best in building transition team effectiveness in M&A?

Combating Culture Clash

Just as an organization cannot effectively run with multiple incompatible information systems, it cannot succeed with multiple incompatible cultures. But successful combinations do not require the partners to be “cultural clones.” In fact, a moderate degree of distinction between the partners’ cultures results in the most successful integrations – the parties have sufficient enough similarities to take advantage of the differences, but they are not so disparate as to be like “oil and water.”

A key question, then, is what drives a culture clash toward conflict versus synergy? Social identity theory suggests that people show a positive bias toward members of their own group and tend to hold a negative view about the members of an “out-group” in order to enhance the relative standing of their own kind (Tajfel, 1981; Turner, 1982). The in-group bias and “us-versus-them” comparisons are likely to be greatest when there is a perceived external threat, such as that posed by a combination.

A contrasting point-of-view is that cultural differences can be a source of value creation and learning. This perspective is largely based on the assumption that differences rather than similarities between combining organizations create opportunities for synergies and learning (Vermeulen & Barkema, 2001). Cultural differences, it is argued, can break rigidities in acquiring firms, help them to develop richer knowledge, and foster innovation and learning.

Research Question 2f. When do cultural differences contribute to versus detract from combination success?

A survey of CEOs who had attempted combinations found that “the major factor in failure was the underestimation of the difficulties of merging two cultures” and another study found that, while 80% of senior executives felt underprepared to deal with culture, those that did give early attention to it were more likely to realize synergies (Kelly, 2006). In a field study, Schweiger and Goulet (2005) examined three levels of cultural learning during an acquisition – none, shallow, and deep – and found an interesting relationship between them and the subsequent integration of plants in an acquired firm. In the case of no learning, they found, not surprisingly, no relationship to eventual integration success or failure. By contrast, deep culture learning interventions, involving cross-company dialog, culture clarification workshops, and the like, had a strong, positive effect on integration success. Measured results included greater cross-cultural understanding, smoother resolution of cultural differences, more communication and cooperation between combining parties, and greater commitment to the combined organization. What fascinates in this study is that shallow learning – for example, show-and-tell presentations, official communiqués, informal Q&A, and such – did little to clarify and eliminate inaccurate cultural stereotypes or to reconcile differences between the partners. On the contrary, these had the undesirable effects of strengthening perceptions of cultural differences and reinforcing stereotypes that contributed to conflict between the organizations.