CHAPTER 2: LITERATURE REVIEW

Introduction

Background

Corporate acquisitions represent part of a corporate/business strategy used by many firms to achieve various objectives. For example, acquisitions can be used to penetrate into new markets and new geographic regions, gain technical/management expertise and knowledge, or allocate capital. In order to survive and grow, business organizations often utilize mergers and acquisitions strategically. However, many poorly understood and managed acquisitions result in disappointing performance, and up to 50 percent are regarded as generally unsuccessful (Business Week, 1985; Louis, 1982). Moreover, according to Mercer Management Consulting (Cited in Smith & Hershman, 1997), in the 1990s the success rate of corporate acquisitions is barely 50 percent, and in the 1980s, 57 percent of acquisition deals failed.

To date, U.S. corporations utilize acquisitions as one of the most frequently selected instruments for growth. Sophisticated and systematic corporate acquisitions research can help acquirers' pre-acquisition understanding and post-acquisition performance, as well as in achieving other acquisition objectives. However, Sirower (1997) stated that, "despite a decade of research, empirically based academic literature can offer managers no clear understanding of how to maximize the probability of success in acquisition programs" (p. 13). Understanding the sources and/or determinants of value creation or value loss is vital to comprehending the causes of success and failure of corporate acquisitions.

This literature review not only attempts to collect and categorize previous research, but also attempts to analyze and evaluate previous works leading to this study's framework, as discussed in the preceding chapter.

Chapter Preview

This study focuses on the discovery and examination of the determinants of successful acquisitions in the hotel industry. This chapter comprises a review of relevant literature. The review begins with an identification of previous acquisition research paradigms, and the evolution of corporate acquisitions and its relationship to corporate strategies. This is followed by an identification of overall, post-acquisition performance. Then, there is a discussion of the causes and objectives of corporate acquisitions. The next section deals with influences and problems in the overall acquisition management processes. This section also will explore details of the key factors involved in both the pre- and post-acquisition management processes. The chapter concludes by identifying appropriate measurement criteria for post-acquisition performance.

Corporate Acquisitions and Their Research Paradigms

Datta, Pinches & Narayanan (1992) identified two primary literature frameworks for identifying sources of shareholders' wealth in acquisition activities, including: strategic management and financial economics literature, which have somewhat different research directions.

Strategic management researchers have primarily attempted to emphasize factors what are management controlled. For example, they have attempted to identify differences between types of diversification strategies (i.e., related vs. unrelated diversification) as a crucial factor in determining post-acquisition performance. The other areas of interest in corporate acquisition research are (1) attempts to identify differences between types of acquisition (i.e., merger vs. tender offer); and (2) attempts to identify differences between types of payment (i.e., cash vs. stock). On the other hand, financial economists have attempted to substantiate their unique viewpoint, the so-called "market for corporate control." The core argument of this "market for corporate control" paradigm is that acquisition activities are viewed as "contests between competing management teams for the control of corporate entities" (p. 69, Datta et al.). One of the key arguments of the market for the corporate control paradigm is that economic value created through acquisition activities is decided by market characteristics, including its competitiveness (e.g., number of acquisition bidders and regulatory changes affecting a particular market).

However, the above two approaches have not been able to explain, exactly, the sometimes disappointing outcomes in corporate acquisitions. Thus, many researchers have begun to attempt to identify crucial variables that related to the disappointing results identified in many acquisition studies, through investigating the relationship between post-acquisition integration and post-acquisition performance. Since Kitching's (1967) initial notion that the post-acquisition integration process is one of the most important factors for success, it was identified that value creation from acquisitions are gained not only from those strategic factors that cause realization of synergies as reflected in capital market expectations (Chatterjee, 1992; Seth, 1990), but also the processes that lead to the realization of anticipated synergistic benefits to be realized (Datta, 1991; Jemison, 1988). In sum, the key topic of this research paradigm is that one of the most crucial issues to be dealt with in corporate acquisitions is the inquiry into how the acquirer and target firms are to be integrated in the post-acquisition management process.

Evolution of Acquisitions and it's Relationship with Corporate Strategy

In order to improve the understanding of corporate acquisition trends, this study has attempted to identify the past and current trends of mergers and acquisitions in the United States and its incorporation with corporate strategy. Four significant merger waves occurred in the United States prior to the 1990s: the mergers of the late 1890s, those of the 1920s, those of the 1960s, and those of the 1980s.

The First Wave, 1897-1904. The first merger wave occurred after the Depression of 1883, peaked between 1898 and 1902, and ended in 1904. Because the first wave involved predominantly horizontal acquisitions, this caused a surge in industrial stocks and resulted in the creation of monopolies. Some of today's huge industrial corporations originated in the first merger wave, including Du Pont, Standard Oil, General Electric, Eastman Kodak, and American Tobacco (Gaughan, 1996).

Table 2. First Merger Wave

Year	**Number of Mergers**
1897	69
1898	303
1899	1,208
1990	340
1901	423
1902	379
1903	142
1904	79

[Source: Merrill Lynch Business Brokerage and valuation, Mergerstat Review, 1989]

The Second Wave, 1916-1929. The second merger wave was termed "merging for oligopoly," whereas the first wave was termed "merging for monopoly." The second wave occurred from around 1925 to the end of decade, and most mergers from this period were characterized as horizontal or vertical integrations (Jemison & Sitkin, 1986[1]). An abundant availability of capital was fueled by favorable economic conditions and lax margin requirements. The antitrust law force of the 1920s was stricter than the period of the first merger wave. With a more strict environment, the second merger wave created fewer monopolies, but more oligopolies and many vertical integrations (Gaughan, 1996).

The Third Wave, 1965-1969. The 1960s, which have been termed the decade of conglomerates, saw the most controversial of the acquisition activities. The conglomerates, such as Textron, ITT, and Litton, or "empire builders," acquired many unrelated business firms in order to reduce cyclical risks. Conglomerates not only grew rapidly, but also profitably, and top executives of these conglomerates were perceived as breaking new ground. According to Judelson (1969), these management skills facilitate a necessary unity and compatibility among a diversity of operations and acquisitions. For example, ITT acquired a variety of business firms, such as rental cars, insurance, wood pulp, and bread companies. Harold Geneen, a chaiman & CEO of ITT, used a system of detailed budgeting, tight financial control, and face-to-face meetings among his general managers to build ITT into a highly diversified, but well-functioning conglomerate (Geneen, 1984). In the third wave, the most typical payment method was in stocks.

Table 3. Third Merger Wave

Year	Number of Mergers
1963	1,361
1964	1,950
1965	2,125
1966	2,377
1967	2,975
1968	4,462
1969	6,107
1970	5,152

[Source: Gaughan, 1996]

The most important notion for diversified firms is the argument that the top executives of these firms possess general management skills that aim at contributing to the overall performance of the firm. According to Andrews (1969), there has been a continuous growth of management talent in America, equal to the task of managing diversity. The divisionalized structure of large companies provides the opportunities for younger managers to gain the requisite experience. Andrews (1951) further argued that general management skills contributed to diversification, helping to create "successful diversification—because it always means successful surmounting of formidable administrative problems—develops know-how which further diversification will capitalize and extend" (p. 98). Goold & Luchs (1993) stated that, "The idea that professional managers possessed skills that could be put to good use across different businesses rested on the assumption that different businesses nevertheless required similar managerial skills" (p. 8).

During the 1960s, most research focused on identifying the basic management principles valuable to all kinds of managers and corporations (Goold & Luchs, 1993). Drucker (1955) argued that "intuitive" management was no longer competitive. Drucker further advocated that managers should cultivate management principles, acquire knowledge, and analyze their performance systematically. Koontz (1961) outlined the management process school, which aimed to identify universal management principles, and held the greatest promise for accelerating management practices. Both Drucker's and Koontz's arguments "naturally emphasized the issues and problems which were common across different types of businesses, since their aim was to help all managers improve their skills and the performance of their businesses" (p. 8, Goold & Luchs, 1993). Berg (1969) stated that corporate strategies based upon improving the performance of a diverse collection of business would have important implications for management practices, and also for public policies. Goold & Luchs (1993) stated that, "There was little reason to question the belief that general management skills provided a sufficient rationale for diversified companies while such corporations were performing well and growing profitably" (p. 10).

However, by the late 1960s, conglomerates began to experience performance problems. In early 1969, the share prices of such conglomerates, including Litton, Gulf &Western, and Textron, fell almost 50 percent from their hey days, compared to a 9 percent drop in the Dow Jones Industrial Average over the same period. Even ITT's consistent record of increased quarterly earnings over 58 quarters during the 1960s and 1970s was broken in 1974 (Bonge & Coleman, 1972). Goold & Luchs (1993) pointed out the causes of the decline of the conglomerates era as "What became apparent was that sound principles of organization and financial control, coupled with a corporate objective of growth, were not, alone, sufficient to ensure satisfactory performance in highly diversified companies" (p. 10). Further, Goold & Quinn (1990) stated that even General Electric realized by the early 1970s what it called a "profitless growth." That is, GE's sales increased 40 percent from 1965 to 1970, whereas its profits actually dropped.

The era of the conglomerates ended with ITT's 1995 spin-off into three different companies (Sikora, 1995). It can be said that most of the conglomerates' merger strategies failed, and they jettisoned their unrelated or under-performing companies in order to maintain their strengths in today's stiff competition. According to Sadtler, Campbell, & Koch, the combined value of firms jettisoned from their parent companies substantially increased from $17.5 billion in 1993, to more than $100 billion in 1996 in the U.K. and in the United States (Economist, 1997).

In the lodging industry, in 1954, the historical merger between Hilton and Statler stunned the entire lodging industry. The lodging industry also experienced turbulent changes in the 1960s. Following the trend of conglomerates' acquisitions of unrelated businesses, some hotel firms became the prey of empire builders. For examples, TWA acquired Hilton International, which operated in 42 countries outside of the United States, and ITT took over Sheraton Corporation's 160 hotels. Also, with acquiring 576 Big Boy Franchises in 1967, Marriott became the nation's largest commercial food and lodging firm, with sales of approximately $383 million in 1968. It executed its initial public offering (IPO) in the same year. One of the most important trends of the 1960s was that many international airline companies had already acquired or were trying to take over hotel/motel firms (The Cornell HRA Quarterly, 1968).

Acquisitions and Corporate Strategy in the 1970s. The number of merger and acquisition transactions in the 1970s fell dramatically (See Table 4).

Table 4. M&A Announcements in the 1970s

Year	Number of Mergers
1971	4,608
1972	4,801
1973	4,040
1974	2,861
1975	2,297
1976	2,276
1977	2,224
1978	2,106
1970	2,128
1980	1,889

[Source: Merrill Lynch Business Brokerage and valuation, Mergerstat Review, 1989]

As a consequence of the problems by conglomerates experienced showed in the 1970s, there was increasing attention paid to the effectiveness of the concept of general management skills. One of the emerging concepts during the 1960s and 1970s was the need for top executives to focus their attention on the long-term goals of their firms. As Chandler (1962) said, strategy is the determinator of the basic long-term goals of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out these goals. Further, Christensen (1965) argued that the concept of strategy made it possible to simplify the complex tasks of top executives. It was increasingly emphasized that the top management tasks are to identify and set up their firms' long-term objectives, rather than the control of the day-to-day operations of their strategic business units. More and more CEOs accepted that strategy must be their primary and unique task.

Andrews (1971) defined the primary task of corporate strategy as identifying the businesses in which the firm would compete, an idea that became a generalized understanding of corporate strategy. However, corporate strategy did not provide practical guidance to some of the problems faced by diversified firms. Specifically, Goold & Luchs (1993) stated that, corporate strategy "did not help them decide how resources should be allocated among businesses, especially when investment proposals were being put forward by a large number of disparate businesses, each with its own strategy. This problem was exacerbated when the aggregate demand for resources exceeded what was available" (p. 11).

Bower (1970) argued that investment decisions should not be made on a project-by-project basis, but had to be integrally related to a business's strategic product and market decisions. In the 1970s, portfolio planning was developed by Boston Consulting Group, and then widely accepted as a solution to solve practical problems of resource allocation in the context of an overall corporate strategy. Portfolio planning provided managers with a common framework to compare many different businesses. During the 1970s, many firms adopted portfolio planning as their fundamental management principle. For example, one survey showed that by 1979, 45 percent of the Fortune 500 companies used some form of portfolio planning (Haspeslagh, 1982). Goold & Luchs (1993) stated that, :the key concept here was the idea of a balanced portfolio: made up of businesses whose profitability, growth, and cash flow characteristics would complement each other, and add up to a satisfactory over corporate performance" (p. 11).

However, as time passed, problems associated with portfolio planning emerged. As Goold & Luchs (1993) stated:

> "Companies discovered that while certain businesses appeared to meet all the economic requirements of the corporate portfolio, they did not fit easily into the corporate family. It turned out to be extremely difficult, for example, for corporate managers with long experience of managing mature businesses in a particular industry sector to manage effectively their acquired growth businesses in new, dynamic, and unfamiliar sectors" (p. 12).

In search for solutions to the problems of portfolio planning, Haspeslagh (1982) found that firms made few changes in their formal corporate systems, but corporate managers in successful firms did make informal attempts to adapt these systems to their business strategies. Furthermore, Hamermesh & White (1984) found that administrative context was an important factor in explaining business performance, and that many firms were taking the wrong approach to some of their businesses. Goold & Luchs (1993) pointed out these identifications as "The recognition that different types of businesses had to be managed differently undermined the argument that general management skills, buttressed by the common frameworks of strategy and portfolio planning, provided the rationale for diversified companies" (p. 13).

The Fourth Wave, 1981-1989. In the 1980s, another merger wave occurred in the U.S. business world. Sikora (1995) expressed this phenomenon as "A highly skilled service infrastructure of investment bankers, lawyers, tax experts, due diligence probers, valuation mavens, and even environmental specialists developed to skipper buying and selling through the gritty M&A process. Shareholder value motivations leaped to the forefront, triggering both acquisitions and sell-offs" (p. 50). The total value of the mergers of the 80s was approximately $1.3 trillion. In the 80s, merger deals were larger and more frequent than ever. Some driving forces behind this phenomenon were: financial shoppers, equipped with substantial support from lenders and investors, were able to acquire a variety of larger deals than ever; globalization facilitated foreign companies' pouring their money into the U.S. market; enough funds were available to support a number of buyout deals; and, the antitrust law was lenient (Sikora, 1995). Moreover, previous researchers identified the causes of the fourth merger wave as excess capacity (Jensen, 1993), agency problems (Jensen, 1988; Lichtenberg & Seigel, 1989), market failure (Shleifer & Vishny, 1991), and tax and antitrust law changes (Bhagat, Shleifer & Vishny, 1990).

During the 1980s, there was almost unanimously skeptical agreement about diversified firms' capacity to create value. As Goold & Luchs (1993) expressed, "The takeover activity of the 1980s prompted a re-thinking of both the role of corporate management in large companies, and of the kinds of strategies which were appropriate for diversified companies" (p. 13). In the 1980s, in order to survive, U.S. companies cut costs and downsized their staffs, but this was not sufficient to create value for their firms. Porter (1987) found that the diversification strategies of many U. S. firms had failed to create value.

More importantly, during the 1980s, American CEOs changed their fundamental goals from building empires to creating shareholders' value. Goold & Luchs (1993) stated that, "Managers were encouraged to evaluate corporate performance in the same terms as the stock market (and raiders), using economic rather than accounting measures, and to take whatever actions were necessary to improve their company's stock price" (p. 14). Rappaport (1986) and Reimann (1987) argued that value-based planning, through adopting the financial tools of discounted cash flow, ROE spreads, and hurdle rates, provided business managers with a different perspective on the link between competitive advantages and stock prices. Both Rappaport and Reimann's assertion is that a firm's share price is determined by the value of a firm's level of competitive strategies.

However, some flaws of value-based planning were revealed in its use as for a framework to corporate strategy. As Goold & Luchs (1993) pointed out "It can help corporate managers to focus on the goal of increasing shareholder wealth and to understand the criteria that must be met to do so. It does not, however, provide much insight into the kind of corporate strategies that should be pursued to meet these criteria. A higher stock price is a reward for creating value. But the key question remains: how can corporations add value to a diverse business portfolio?" (p. 14).

During the 1980s, the primary underpinning concept of successful corporate strategy was based upon core business, or "stick to the knitting." According to Peters & Waterman (1982), successful firms did not diversify into various businesses. They tended to specialize in their core businesses and focused on improving their knowledge, including their expertise and management skills in the areas they knew best. Moreover, Hayes & Abernathy (1980) argued that most American companies were being run by professional managers, who specialized in finance and law, but were lacking in technological expertise or in-depth particular industry experience. The authors cautioned that portfolios of diversified firms across dissimilar industries and businesses were fit for stocks and bonds, but not for corporations. Mintzberg (1989) also attacked the concept of a portfolio planning matrix by stating the need for “focused corporations that understand their missions, ‘know’ the people they serve, and excite the ones they employ; we should be encouraging thick management, deep knowledge, healthy competition and authentic social responsibility” (p. 373). The growing attention of specialized firms to these concepts clearly contrasted with the existence of diversified firms’ ability to create value from their portfolio of businesses.

In order to survive, many huge American companies had to adopt a restructuring strategy. Restructuring involved the disposal of corporate assets, and was regarded as a salutary correction to the excesses of extensive diversification. Jensen (1989) argued that corporate break-ups, divisional sell-offs, and LBOs are crucial developments that can prohibit the unproductive use of capital by managers of large firms. Since the 1980s and to the present, there has been a trend towards increased specialization. Denis, Denis & Sarin (1997) identified the causes of this refocused strategy as “decrease in diversification is typically prompted by external control threats, financial distress, and management turnover suggesting that, in general, firms do not voluntarily refocus in order to adapt to environmental change. Rather, refocusing appears to be the result of external monitoring of managerial behavior” (p. 80).

In the lodging industry, some notable leveraged buyout (LBO) transactions occurred during the 1980s. According to Moncarz (1991), in February 1985, Kohlberg, Kravis, Roberts, and Company (KKR) and a new management team converted Motel 6s public firm to a private one, with the exchange of some $881 million (including $125 million in equity and $756 million of debt). However, in July 1990, Accor S.A., a French lodging giant, acquired Motel 6 for 1.3 billion in cash, a very high rate of return. Moreover, in 1990, Days Inn agreed to be acquired by Tollman Hundley Corporation for $765 million ($90 million in cash and the assumption of $675 million of debt). However, the new owner experienced a difficult time due to the enormous amount of debt, because of the high burden of its interest rate.

As a summary of the merger activities of both the 1960s and the 80s, it can be assumed that diversification and conglomeration were the dominant acquisition trends in the 1960s, whereas consolidation and specialization were the most common phenomena of the 1980s. Shleifer & Singh (1994) stated that: “The fact that diversification of the 1960s did not, on average, lead to profitability improvements and was, to a substantial extent, subsequently reversed, is clear evidence of a failure that was not expected in the 1960s," (p. 406) and, "In the 1960s, conglomerates were created; in the 1980s, many of them were destroyed" (p. 408).

The Current Wave, 1990-Present. The predominant M&A deals of the 1990s are carefully designed to secure a strategic fit between merging firms. In the 1990s, the merger wave was shaped very differently than that of the 1960s, the decade of the "conglomerates," and that of the 1980s, the decade of the "leveraged buyouts" (LBOs). Lipin (1997) pointed out that, "Except that it isn't really like those eras. It is bigger, for one thing. And the forces behind it are different" (p. A1). For example, in 1996, for the first time, each of the top 100 deals was a megadeal, worth more than $1 billion or 53.5 percent of the total transactions (Sikora, 1997).

Table 5. Mergers & Acquisitions Completions from 1980 to 1996

	Hotels and Casinos*		All Industries		
		(A)		(B)	(A) / (B)
Year	***# of Deals***	***Value** ($mil)*	***# of Deals***	***Value ($bil)***	
1980	-	-	1,558	34.8	-
1981	10	561.6	2,328	69.5	0.81%
1982	5	39.4	2,299	60.7	0.06
1983	4	5.6	2,395	52.7	0.01
1984	7	1,180.6	3,176	126.1	0.94
1985	11	993.2	3,490	146.1	0.68
1986	10	493.0	2,523	220.8	0.22
1987	21	2,369.0	2,517	196.5	1.21
1988	15	4,376.0	3,011	291.3	1.50
1989	49	4,450.4	3,825	325.1	1.37
1990	46	3,197.4	4,312	206.8	1.55
1991	19	560.3	3,580	143.1	0.39
1992	22	748.5	3,752	125.3	0.60
1993	44	2,081.1	4,148	177.3	1.17
1994	80	2,701.4	4,962	276.5	0.98
1995	93	4,598.1	6,209	375.0	1.23
1996	166	11,104.2	6,828	550.7	2.02
TOTAL	**602**	**39,459.8**	**60,913**	**3,378.3**	**1.17 (Ave.)**

Source: Mergers & Acquisitions (The provided information is based on all completed mergers, acquisitions, and divestitures priced at $5 million and over, as well as purchases of partial interest that involve at least a 40% stake in the target company or an investment of at least $100 million. Prior to 1991, a transaction was included if it was valued at $1 million or more. Partial acquisitions of 5% or more of a company's capital stock are included if the payments are $1 million or more).

** Mergers & Acquisitions Magazine changed the categorization of the lodging industry over time: 1981-1988: as Hotels & Lodging Places; 1989-1991: as Hotels & Restaurants; and 1992-current: as Hotels & casinos.*

Compared to the 60s and 80s, it could be said that the 1990s is the decade of 'consolidations'. Consolidation means the combination of two firms' operating and management resources, as well as their assets, debt, and stocks (Watson, 1960). Most acquirers have employed acquisition as expansion strategies within their unique industries. These appear to be less risky acquisitions because they were paid for with stock, which is recognized as being less risky than cash, compared to the 80s when payments were made with cash rather than stock. It is generally believed that consolidation tends to be a means of reducing costs and achieving scale economies from acquisitions. There are several driving forces that have facilitated the current merger-mania syndrome. Lipin (1997) claimed that, "the current merger boom, fueled as it is by executives' drive for market share, efficiency, and pricing power in core businesses, bears similarities with an earlier merger wave, at the end of the last century" (p. A1).

Further, the continuation of a stable economic environment, relatively favorable antitrust law enforcement, a low cost of capital, and the stock market's good condition are the catalysts of the current acquisition trend. However, there were still many acquiring companies who failed to generate shareholder value. According to a merger study done by Mercer Management Consulting Inc. (1997), "among all mergers in the 1990s, 48 percent still fail. That compares with 57 percent in the 1980s. But among the largest mergers – when the target company is at least 30 percent of the acquiring company, measured by revenues – the failure rate jumps to 75 percent." Acquirers have been fueled by the notion that firms had to collect larger and larger pools of assets either to survive or to grow.

According to Goold & Luchs (1993), the primary issues for corporate strategy in the 1990s are how to identify the businesses that should form a core portfolio for a firm, and how to discover ways of creating value for those businesses. Goold & Luchs (1993) identified three alternative answers to the above questions. First, diversification must be limited to those businesses with synergy potential. Synergy can be achieved when the performance of a portfolio of businesses adds up to more than the sum of its parts. The most compelling concept of synergy is based in part upon scale economies and the cost saving structure of a portfolio of businesses. Porter (1985) argued that without synergy, a diversified company is nothing but a mutual fund. Moreover, Kanter (1989) also argued that a diversification strategy's only justification is the achievement of synergy. However, both Porter and Kanter acknowledged that firms found it is hard to gain synergy benefits, and therefore there is a high rate of failure. Chatterjee (1992) points out that synergies are hard to achieve and that most acquisition gains arise from asset disposals and restructuring, rather than from anticipated synergistic benefits. Synergy remains a fundamental rationale for acquisitions, but it is difficult to agree that it is the only way to create value in a diversified company. Goold & Luchs (1993) stated that, “The assumption that synergy is the only rationale for a group of companies does not fit the available evidence, and this suggests that not all corporations need to focus their efforts on constructing and managing portfolios of interested businesses” (p. 17).

Second, the corporate strategy must be focused on exploiting core competencies across different businesses and/or industries. Hamel & Prahalad (1990) argued that the corporate portfolio should be considered as a portfolio of technological competencies, rather than a portfolio of businesses. Itami (1987) emphasized building a company’s “invisible assets,” such as a particular technological expertise, brand names, reputation, or customer information. Itami argued that such assets can be utilized throughout the firm without being used up, and they are the most valuable source of sustainable competitive advantage. Haspeslagh & Jemison (1991) defined core capabilities as managerial and technological experience accumulated primarily through a resource-based view of a firm. Such capabilities can be utilized across a firm’s businesses and can make a critical contribution to customer benefits. Haspeslagh & Jemison (1991) also proposed three generic types of acquisition: (1) Domain strengthening; (2) Domain extension (building on existing business); and (3) Domain exploring (going into new markets or technologies). Moreover, Kietel (1988) stated that, “To the extent that such skills can be exploited by each of the company’s businesses, they represent a reason for having all those businesses under one corporate umbrella—a much better reason, the experts add, than the fabled synergies that multibusiness companies of yore were supposed to realize but seldom did” (p. 20).

However, a core competence approach also has flaws. Goold & Luchs (1993) stated that, “It can be difficult to judge when an investment in a business is justified in terms of building a core competence, particularly if it means suspending normal profitability criteria and if the investment is in an unfamiliar business area” (p. 18). Furthermore, Goold & Luchs (1993) stated that, a “competence approach to corporate strategy is that businesses may require similar core competences, but demand different overall strategies and managerial approaches” (p. 18). Goold & Luchs (1993) further stated that, “Corporate executives are concerned not only with building skills and competences in their businesses, but also with allocating resources to them, approving their plans and strategies, and monitoring and controlling their results” (p. 19).

Third, building a collection of businesses which fit with the managerial "dominant logic" of managers and their management style is one of the best ways to diversify successfully. Prahalad & Bettis (1986) argued that, "A dominant general management logic is defined as the way in which managers conceptualize the business and make critical resource allocation decisions—be it technologies, product development, distribution, advertising, or in human resource management" (p. 490). When a manager's dominant logic does not fit the requirements of the business, problems and frustrations can arise. Goold & Luchs (1993) stated that, "Dominant logic may help explain why conglomerate diversification can succeed, and also why diversification based on synergy or core competences can fail. If conglomerate diversification, such as that of Hanson, is based on businesses with a similar strategic logic, then it is possible for corporate management to take a common appproach and to add value to those businesses. On the other hand, businesses with opportunities for sharing activities or skills, or ones requiring the same core competences, may nonetheless have different strategic logics. This makes it difficult for corporate management to realize synergy or exploit a core competence across the businesses" (p. 20). It was identified that firms are inclined to utilize a specific management style, and that it was difficult to for executives to deal with a wide variety of approaches and styles (Goold & Campbell, 1987). Moreover, Prahalad & Doz (1987) argued that the successful firms in global competition will be those firms that can develop differentiated structures, and management processes and systems appropriate to the wide range of their businesses.

Evidence of Post-Acquisition Performance

There are many studies that have attempted to identify outcomes about corporate acquisitions, in terms of stock returns, to determine whether or not they created additional value for the acquiring firms' shareholders. The results were mixed. In terms of aggregate post-acquisition performance, some studies found that there were significantly negative returns to the acquirers (Dodd, 1980; Eger, 1983; Firth, 1980; Malatesta, 1983), whereas other studies reported significant abnormal returns for the acquiring firms (Asquith, Bruner & Mullins, 1983; Chung & Weston, 1982). More specifically, through the study of the long-run performance of acquirers after acquisitions, some studies found that acquiring firms experienced significantly negative abnormal returns over the one to three year period after the acquisition (Langetieg, 1978;

Asquith, 1983; Magenheim & Mueller, 1988). Futher, Agrawal, Jaffe & Mandelker (1992) confirmed that acquiring firms experienced a loss of 10 percent over the five years after the acquisition completion.

Much of the previous research has investigated the relationship between types of acquisition, such as related acquisition, unrelated acquisition, and vertical acquisition, and the firm's performance based upon the results of accounting profits and stock returns, but has not addressed the causes of success. Corporate acquisitions and the firm's performance has attracted the interest of many researchers. However, the results of investigation of related and unrelated diversification were mixed. Rumelt (1982) found that related acquisitions showed a higher profitability than unrelated diversification, and this finding was further replicated by others (Christensen & Montgomery, 1981; Lecraw, 1984; Varadarajan & Ramanujam, 1987).

However, other studies found that unrelated acquisitions outperformed related acquisitions (Weston, Smith & Shrieves, 1972; Mason & Goudzwaard, 1976; Michel & Shaked, 1984; Dolan, 1985; Luffman & Reed, 1984). Furthermore, some studies found no significant performance differences among types of acquisition strategies (Grinyer, Yasai-Ardekani & Al-Bazzar, 1980). In fact, many studies ignored the exact causes of the successful corporate acquisition modes because the results were mixed, as shown above, so that one could not deduce the determinants of such successes in terms of an effective overall acquisition process. More specifically, horizontal acquisitions are more closely associated with higher synergy than conglomerates and vertical acquisitions and, thus have the potential to outperform the latter (Chatterjee, 1986; Porter, 1985; Rumelt, 1974). However, other studies show that conglomerates and vertical acquisitions outperformed horizontal acquisitions (Kitching, 1967; Lubatkin, 1987).

According to Loughran & Vijh (1997), there are three typical results from numerous previous studies. First, the target firm's stockholders gained significantly higher abnormal returns from all acquisitions. Second, the acquiring firm's stockholders gained little or no abnormal returns from all tender offers. Finally, the acquiring firm's stockholders gained negative abnormal returns from all merger transactions (Dodd & Ruback, 1977; Kummer & Hoffmeister, 1978; Dodd, 1980; Asquith, 1983; Bradley, Desai & Kim, 1983; Jensen & Ruback, 1983; Malatesta, 1983).

In general, it is believed that the overall result of acquisitions is negative rather than positive, as Ruback (1988) said, "Reluctantly, I think we have to accept this result—significant negative returns over the two years following a merger-as a fact" (p. 262). Moreover, Jensen & Ruback (1983) pointed out that, "These post-outcome negative abnormal returns are unsetting because they are inconsistent with market efficiency and suggest that changes in stock prices during takeovers overestimate the future efficiency gain from mergers" (p. 20). Agrawal, Jaffe & Mandelker (1992) pointed out that:

> "A finding of underperformance has three important implications. First, the concept of efficient capital markets is a major paradigm in finance. Systematically poor performance after mergers is, of course, inconsistent with this paradigm. Second, much research on mergers examines returns surrounding announcement dates in order to infer the wealth effects of mergers. This approach implicitly assumes that markets are efficient, since returns following the announcement are ignored. Thus, a finding of market inefficiency for returns following mergers calls into question a large body of research in this area. Third, a finding of underperformance may also buttress certain studies (e.g., Ravenscraft & Scherer (1987) and Herman & Lowenstein (1988)) showing poor accounting performance after takeovers. However, the evidence is not one-sided here (see, e.g., Healy, Palepu, and Ruback (1992)" (p. 1606).

Most recently, Mercer Management Consulting found that, "since the mid-'80s, 57 % of deals worth $500 million or more resulted in poor returns to shareholders during the three years following the acquisition, relative to the industry average. Even in the 1990s, when deals tend to be more closely linked to the acquiring company's core strategy, the success rate is barely 50%" (p. 39, Cited in Smith & Hershman, 1997).

Causes of Corporate Acquisitions

Most researchers agreed that corporate acquisitions are complex phenomena forced by various patterns of acquisition motives, and that no single theory can explain a comprehensive account (Steiner, 1975; Ravenscraft & Scherer, 1987). There are many assertions that have been made about why firms acquire other firms or competitors. This section will identify some of the dominant perspectives discussed by many researchers. This section will be divided into two parts, including: 1) theories of corporate acquisitions; and 2) objectives and/or motives of corporate acquisitions.

<u>Theories of Corporate Acquisitions</u>

The first category of why firms acquire other businesses can be phrased as the question: Why do firms diversify? Based upon a synthesis of previous studies, Montgomery (1994) stated three types of diversification theories, including: the market-power view, the agency view, and the resource-view. According to Hill (1985), the market power view argued that diversified firms will "thrive at the expense of nondiversified firms not because they are any more efficient, but because they have access to what is termed *conglomerate power*" (p. 828). Through utilizing some economists' assertions, Montgomery introduced three ways in which conglomerates could create power in an anti-competitive way: "cross-subsidization, wherein a firm uses its profits from one market (sometimes known as "deep pockets") to support predatory pricing activities in another; mutual forbearance, where competitors meeting each other in multiple markets recognize their interdependence and complete less vigorously; and reciprocal buying, where the interrelationships among large diversified firms foreclose markets to smaller competitors" (p. 165).

In terms of the agency view, in relation to Montgomery's article, Morck, Shleifer & Vishny (1988) pointed out "When managers hold little equity in the firm and shareholders are too dispersed to enforce value maximization, corporate assets may be deployed to benefit managers rather than shareholders" (p. 293). With the fragmentation of an owners' inability to monitor their agencies (managers) effectively, managers pursue their own interests at the firm's owners' expense, rather than pursuing profit maximization for the firm (Jensen, 1986). Another agency viewpoint is that managers prefer the firm's growth, rather than profitability.

Finally, the resource view insisted that, according to Montgomery, in order to gain abnormal rent, firms diversify in response to an excess capacity in productive resources, both tangible and intangible. In Montgomery's article, Penrose (1959) stated that the attainment of such a 'state of rest' (equilibrium position) is precluded by three significant obstacles: "those arising from the familiar difficulties posed by the individuality of resources; those arising from the fact that the same resources can be used differently under different circumstances, and in particular, in a 'specialized' manner; and those arising because in the ordinary processes of operation and expansion new productive services are continually being created" (p. 68). Moreover, Barney (1988) stated that "in order to obtain expected above-normal returns from acquisitions, firms must complete acquisitions in only imperfectly competitive markets for corporate control" (p. 78). Wernerfelt (1984) further supported a resource-based view by saying that "an acquisition can be seen as a purchase of a bundle of resources in a highly imperfect market. By basing the purchase on a rare resource, one can ceteris paribus maximize this imperfection and one's chances of buying cheap and getting good returns" (p. 172). Salter & Weinhold (1979) stated that a set of acquisition strategies based on a resource-based view of the firm includes (1) related supplementary (acquire the same resources you already possessed); and (2) related complementary (acquire different resources than what the target has if they can be combined easily with the acquirer's current resources). According to Barney (1988), abnormal returns can be created for the acquirer in combination with the target if the synergistic relationship is not easily copyable by competitors. Moreover, Harrison, Hitt, Hoskisson, & Ireland (1991) found that "different but complementary resource flows may be more likely to create a unique and private synergy than similar resource flows" (p. 187). In sum, a firm's unique, rare and valuable resources captured and accumulated through acquisition strategies, should be matched with its suitable organizational form in order to realize the maximum strategic effectiveness of a united company.

Salter & Weinhold (1979) identified three clusters of theories in corporate acquisitions, including: the strategy model, the product/market portfolio model, and the risk/return model. First, Salter & Weinhold argued that the most general and most established set of theories stems from notions of corporate strategy and corporate planning based upon some notable individuals, such as Adrews, Ansoff, and others. The author indicated distinctive characteristics of the strategy model by saying that, "the key relationship stressed in the strategy model is the relationship between a business enterprise and its environment" (p. 49). This well-known concept is called later a "strategic fit" model in the strategic management arena. Regarding diversification, this model implied that only after a company's strengths and weaknesses in each functional area have been realized, is its top management team able to begin considering the company's future needs and the potential of pursuing diversification through acquisitions. Furthermore, this model suggests that the purpose of diversification through acquisition is not to begin to establish measures of product/market attractiveness, but rather to identify their unique strengths that may be exchangeable in other markets. Ultimately, this model indicated that a firm’s distinctive capabilities can be enhanced or extended by entering into new market areas through acquisition (Salter & Weinhold, 1979).

Second, the product/marker portfolio model emphasized the long-term economic stability and strength of a portfolio of different businesses in the cash flow balance. This model was well represented in the famous product/market portfolio model developed by the Boston Consulting Group (BCG). A particular difference of this model compared to the strategy model is that this model inherently implied for unrelated diversification because it primarily focused on economies of scope. Neither the strategy nor the product/market models were considered to manage the risk issue accompanied by acquisition investments (Salter & Weinhold, 1979). Third and finally, unlike the former two models, the risk/return model was developed and utilized for investors, rather than for operating executives. One of the distinctive characteristics of this model is the risk-return tradeoff of a particular capital asset. That is, the potential acquisition plan for a diversification should be considered as an investment decision. The key concept here is the free cash flow and systematic risk of the target firm, and its impacts on the risk/return structure of the acquirer as well as cost of a diversification through acquisition.

Trautwein (1990) identified seven theories of acquisition motives based upon three clusters, including: 1) acquisition as rational choice; 2) acquisition as process outcome; and 3) acquisition as macroeconomic phenomenon. Rational choice can be classified into two parts, including acquisition aims either for shareholders’ value or managers’ personal goals. The seven acquisition motives identified by Trautwein (1990) are:

(1) Efficiency theory. This concept held that acquisitions were executed to achieve synergies. Three types of synergies are identified. First, financial synergy aimed for achieving a lower cost of capital through lowering the systematic risk of the acquirer. Second, operational synergy targeted achieving operational excellence from a combined firm’s operations. Third, managerial synergy was used to enhance a target’s competitive position by transferring management expertise from the bidder to the target. The view of financial synergy has been attacked by saying that there is no evidence for a lower systematic risk or an advantage of internal capital market (Rumelt, 1974; Montgomery & Singh, 1984). It was determined that operational and managerial synergies are rarely motivations for acquisitions (Kitching, 1967; Porter, 1987). Trautwein concluded that the efficiency theory performance is unfavorable.

(2) Monopoly theory. This theory viewed that acquisitions were executed to achieve market power. The implications of this type of acquisition is that conglomerates use it to cross-subsidize products, to limit competition in more than one market simultaneously, and to deter the potential entrance of competitors into its market. These three advantages of the monopoly theory supported the idea of a collusive synergy (Chatteree, 1986) or competitor interrelatonships (Porter, 1985). However, there are many studies, including Ravenscraft & Scherer (1987) and Jensen (1984), that showed clearly contradictory results. In sum, Trautwein (1990) concluded that the monopoly theory's overall performance is even worse than that of the efficiency theory.

(3) Valuation theory. This philosophy viewed acquisitions as being executed by managers who have superior information than the stock market about their exact target's unrealized potential value (Steiner, 1975; Holderness & Sheehan, 1985; Ravenscraft & Scherer, 1987). The assumption here is that the acquirer possesses valuable and unique information to enhance the value of a combined firm through purchasing an undervalued target or deriving benefits from combining the target's business with its own. The leveraged buyout can be categorized into this theory. Trautwein (1990) mentioned that one of the most common criticisms about this valuation theory is that it is impossible to acquire accurate and tangible information about the acquisition results, and further stated that "the concept of private information as a basis for mergers warrants further consideration, since it shows a way the problematic assumption of capital market efficiency can be avoided" (p. 287).

(4) Empire-building theory. This theory holds that managers maximize their personal goals, rather than their shareholders' value maximization through acquisitions. This theory stems from Berle & Means's (1933) early study on the relationship between ownership and corporate governance structure. This approach has been discussed and debated in many studies (Baumol, 1959; Marris, 1964; Williamson, 1964; Black, 1989). Trautwein (1990) concluded that "the empire-building theory has to be given the most credit of the theories investigated up to this point" (p. 288).

(5) Process theory. This approach indicated that strategic decisions are described as outcomes of processes governed by bounded rational theory (Simon, 1957), the central role of organization routines (Allison, 1971), or political power in the decision process (Allison, 1971), rather than completely rational choices. Duhaime & Schwenk (1985) identified the limitations of information processing capacities in acquisition decisions. Roll (1986) found that the managers' behavior was over-optimistic in the acquisition decision process. Jemison & Sitkin (1986[1]) proposed a systematic acquisition process perspective. Gaddis (1987) found that political and structural matters affect the acquisition process and outcome, whereas Sales & Mirvis (1984) argued that cultural distances between two companies have enormous impacts on acquisition and the post-acquisition integration process. Trautwein (1990) concluded that "the evidence on the process theory can best be described as ambiguous. The available evidence is largely supportive. At the same time, it is so scarce as to forbid any far-reaching inferences" (p. 289).

(6) Raider theory. Holderness & Sheehan (1985) portrayed the term, "raider," as meaning a person who causes wealth transfers from the shareholders of a target firm. One of the wealth transfer media is abundant compensation after a successful acquisition transaction, called "golden parachute." The primary problem with this assertion is its illogical hypothesis of wealth transfer. In addition to this, there is ample evidence of unfavorable results (Trautwein, 1990).

(7) Disturbance theory. This approach holds that the motives of acquisitions occurred as a result of economic disturbances. According to Gort (1969), economic disturbances cause changes in individuals' expectation and increase the general degree of uncertainty. Thus, they alter the array of individual expectations. Trautwein (1990) commented that this theory is no longer examined.

In sum, Trautwein (1990) argued that among the seven competing theories, the valuation theory, empire-building theory, and process theory are the most plausible ones, in the order introduced. The author also argued that the most dominant theory, the efficiency theory, has produced only limited validity.

Pfeffer (1972) argued, based upon Thompson's (1967) viewpoint, that merger is one possible strategy for a firm in order to gain control of environmental interdependence, the so called "resource dependence" theory. Thompson stated that organizations are contingent upon their external environments, therefore, they should try to gain control over their processes of input resource acquisition and output disposal. Thompson & McEwen (1958) further argued that in order to minimize uncertainties initiated from the external environment, organizations seek to develop such strategies as competitive and cooperative strategies, with the latter including three sub-strategies: bargaining, co-opting, and coalitions. Furthermore, Pfeffer argued that, "there also exists the possibility for organizations to deal with uncertainty or interdependence by absorbing it completely through merger." (p. 384). Pfeffer further indicated three points. The first is that organizations may adopt merger as an instrument for integration through merging with either forward or backward partners. The second is that organizations may buy competitors "as a way of reducing competitive or commensalistic interdependence" (p. 384). The final point is that companies may try to manage interdependence through a merger or diversification growth strategy. In summary, some of the examples of lines of thought about the causes of corporate diversification are: inter-organizational dependence (environment), competitive forces, diversification for growth, managers' private interests, economic profits maximization, and acquire valuable resources.

Even though it is not a formal theory, another viewpoint of acquisition phenomena is as seeing it as a "fashion." To date, it seems as though many acquirers "jump on the bandwagon" together. As Maister (1997, cited in Kahan) mentioned, "The reason why mergers are so seductive is because it's the White Knight theory. Everyone hopes that if we merge with those other guys, they will be energetic enough and I'll be able to cruise. But unfortunately, the other guy is thinking the same way" (p. 42).

Motives and/or Objectives of Corporate Acquisitions

Martin & McConnell (1991) identified that there are two broad motivation categories for value maximizing corporate acquisitions. The first is a synergistic acquisition, in that takeover benefits are realized through efficiency gains from combining the operational units of the acquirer and the target. The second is a disciplinary acquisition, where takeover benefits are achieved by replacing the target firm's inferior management team in order to improve its operating strategies. The authors further stated that the takeover market plays a pivotal role in disciplining corporate executives. This role is twofold. First, potential acquirers' continuous monitoring efforts to identify potential prey for a takeover bid is considered as a threat to non-value adding managers. This attempt forces managers to stick with their incentives to increase shareholders' value. Second, when this potential takeover threat does not affect the value depleting managers of the target firm, the actual acquisition attempt corrects their nonvalue-maximizing behavior, through replacing them by the acquirer.

Corporate acquisitions are the principal vehicles by which firms enter new product markets and expand the size of their operations (Saletr & Weinhold, 1979). Ansoff, Brandenburg, Portner, & Radosevich (1971) identified thirteen motives for engaging in acquisitions by U. S. manufacturing firms, as shown in Table 6.

Table 6. A List of Acquisition Motives

1. A desire to limit competition or achieve monopoly benefits
2. A desire to utilize unutilized market power
3. A response to shrinking opportunities for growth and/or profit in one's own industry due to shrinking demand or excessive competition
4. A desire to diversify to reduce the risks of business
5. A desire to achieve a large enough size to realize an economical scale of production and/or distribution
6. A desire to overcome critical lacks in one's own company by acquiring the necessary complementary resources, patents, or factors of production
7. A desire to achieve sufficient size to have efficient access to capital markets or inexpensive advertising
8. A desire to utilize more fully particular resources or personnel controlled by the firm, with particular applicability to managerial skills
9. A desire to displace an existing management
10. A desire to utilize tax loopholes not available without merging
11. A desire to realize the promotional or speculative gains attendant upon new security issues, or changed price earnings ratios
12. A desire of managers to create an image of the themselves as aggressive managers who recognize a good thing when they see it
13. A desire of managers to manage an ever-growing set of subordinates

[From Ansoff, Brandenburg, Portner & Radosevich, 1971]

Management objectives and goals have been studied as a core construct in research on corporate acquisitions (Reid, 1968; Steiner, 1975; Jensen & Ruback, 1983). This research area can be divided into two clusters, including: 1) the development of thorough lists of all the managerial goals and objectives that might motivate management to engage in acquisitions (e.g., Steiner, 1975; Goldberg, 1983); and 2) to emphasize how specific managerial goals motivate involvement in acquisitions (e.g., Williamson, 1975; Lubatkin, 1983; Eckbo, 1983). Some particular objectives were identified, such as market power (Ellert, 1976), operating synergies (Mandelker, 1974), or efficiency (Eckbo, 1986)

Walter & Barney (1986) investigated the objectives and goals motivating management to engage in different types of acquisition activities. Walter & Barney derived and developed a list of 20 possible managerial goals and objectives in involvement in acquisition activities, from numerous authors' previous works (e.g., Kitching, 1967; Howell, 1970; Steiner, 1975) as presented in Table 4. Instead of asking executives directly, Walter & Barney asked questions of professional M&A intermediates, such as professionals in investment banks who had extensive experience in M&As, and who had a valuable network of partners engaged in M&A. Two reasons were identified by the authors focusing intermediaries as respondents. The first was that the authors assumed that an acquiring firm's managers might be not willing to show their intended goals for an acquisition that has not realized those goals, because the goals represent their incentives for stockholders' interest. The second reason is that managers' experience tends to be industry-specific, whereas intermediaries have less biased and broader experience in the M&A arena. These respondents were comprised of M&A specialists in investment banks, venture capitalists, financial advisors, managers of underwriting companies, lawyers, etc. Most of them held high-level positions, such as vice president, president, partner, and chairman. Data were collected through structured interviews that took approximately two hours per transaction. The authors asked respondents to respond to the importance of 20 distinctive objectives for M&A, and then the author performed a cluster analysis. The result of the cluster analysis created five clusters from the above 20 managerial objectives (See Table 7).

Walter & Barney stated the relationship between those 20 objectives and their relevant match for four different categories of M&A. They developed four different categories of M&A types, including vertical, horizontal, concentric, and conglomerate acquisition types (Reid, 1968; Kitching, 1967; Souder & Chakrabarti, 1984). The overall result of the cross-relationship between managerial objectives and types of acquisition is shown in Table 8. Among others, horizontal acquisitions showed that there is no dominant objective, but some co-existing, competing motives were identified. This result is almost equivalent to Chatterjee's (1986) study that concludes that horizontal acquisitions are utilized by acquiring companies for exploiting three distinct types of synergies: collusive synergies, operating synergies, and financial synergies. Unlike this study's result and Chatterjee's argument, the conventional long-lasting belief is that the underlying motives of horizontal acquisition is either "market power theory," or "efficiency theory." Further, concentric acquisition's objectives coincided with Rumelt's (1974) assertion that acquisition is motivated by the acquiring firms' desire for expanding current markets.

Table 7. Managerial Goals for M&A and their 5 Clusters

Managerial Goals for M&A	**Cluster Number**	**Description of Cluster (Objective)**
1. Utilize the acquiring company's expertise in marketing, production, or other areas within the acquired company 2. Create economies of scale by related capacity expansion 3. Utilize the acquired company's personnel, skills, or technology in other operations of the acquiring company	I	Mergers are a way managers obtain and exploit economies of scale and scope
4. Accelerate growth or reduce risks and costs in a particular industry in which the acquiring company has a strength such as executive wisdom 5. Utilize interlocking and mutually stimulating (synergistic) qualities of the acquired company vis-a-vis the acquiring company 6. Improve efficiencies and reduce risk in the supply of specific goods and/or services to the acquiring company	II	Mergers are a way managers deal with critical and ongoing interdependencies with others in a firm's environment
7. Attain improved competitiveness inherent in holding a sizable market share or important market position 8. Reduce risks and costs of diversifying products and services delivered to customers within an industry 9. Penetrate new markets by utilizing the acquired company's market capabilities 10. Improve economies of scale by utilizing the acquired company's distributional capacities to absorb expanded output 11. Broaden the customer base for existing goods and services of the acquiring company 12. Expand capacity at less cost than assembling new facilities, equipment, and/or physical assets	III	Mergers are a way managers expand current product lines and markets
13. Gain valuable or potentially valuable assets with the cash flow or other financial strengths of the acquiring firm 14. Reduce risks and costs of entering a new industry 15. Fulfill the personal ambitions, vision, or some particular goal of the acquiring company's chief executive	IV	Mergers are a way managers enter new business
16. Promote visibility with investors, bankers, or governments, with an eye to subtle benefits later 17. Utilize financial strengths of the acquired company such as foreign tax credits or borrowing capacity 18. Gain complementary financial features such as those that balance earning cyclicality 19. Divest poor-performing elements of the otherwise undervalued acquired company, in portfolio management style 20. Pursue opportunities to sell stock at a profit by such acts as pressing management of the acquired firm for improved earnings	V	Mergers are a way managers maximize and utilize financial capacity

[From Walter & Barney, 1990]

Table 8. The Relation between Different Types of Acquisition and Relevant Managerial Goals

Type of Acquisition	Degree of Importance	Relevant Goals
Vertical	High Low	Manage critical dependencies All others
Horizontal	High Medium Low	None Enter new businesses; Economies of scale and scope; Expand along product lines; Manage critical dependencies Utilize financial capability
Concentric	High Low	Expand along product lines Utilize financial capability
Conglomerate	High Low	Utilize financial capability; Enter new businesses All others

[From Walter & Barney, 1990]

Motives for Horizontal Acquisitions. Some economists argued that industry concentration due to growth dominant firms could allow for efficient production, lower costs, and lower prices (Demsetz, 1973; Peltzman, 1977; Carter, 1978; Ravenscraft, 1984). Therefore, the Justice Department relaxed its restrictions for horizontal acquisitions. Tremblay & Tremblay (1988) stated that, "Appropriate application of the antitrust laws depends upon the motives as well as the effects of mergers. If firms merge to reduce competition, the Justice Department should pursue an antimerger policy. If, however, firms merger to gain efficiencies, a more lenient policy may be desirable" (p. 22). There are some possible motives for horizontal acquisitions.

First, the motive of horizontal acquisition is that efficiency gains through scale economies or market power. However, Stigler (1950) contended that the market power view for acquisition may not be the answer because of spillover effects. The combined entity should bear the cost of combination, and any possible corresponding price increase may cause competitors to extend output. Therefore, competitors earned more benefits from acquisition transactions than the acquiring firm (Tremblay & Tremblay, 1988). Second, Dewey (1961) argued that acquisitions are simply an efficient means of transformation from the failing firm's inferior assets to successful or rising firms. Because of information costs, value-declining firms are unable to find the recipe for success. Therefore, since successful firms possess a better capacity to utilize their industry-specific assets, they tend to purchase failing firms (Tremblay & Tremblay, 1988). Third, Keithahn (1978) argued that rapidly changing technology developments facilitated the scale economies in a particular industry. Fourth, larger firms prefer to utilize growth acquisitions more frequently than smaller firms, because an acquisition is less disruptive to bigger firms' organizational structure (Solow, 1967; Galbraith, 1967). Finally, the business cycle may affect acquisition activities (Link, 1984; Tremblay, 1985).

Tremblay & Tremblay (1988) attempted to verify the above possible motives for horizontal acquisitions in a single industry, the U.S. brewing industry. The authors supported Dewey's hypothesis, and also found that there was no evidence of market power and scale economies. The authors found that larger firms were more likely to be acquirers, and further stated that no explicit cyclical pattern could be found. The authors pointed out that the antitrust laws have efficiently prevented a possible monopoly through acquisitions. Tremblay & Tremblay (1988) stated that, "the recent acceptance of the efficiency defense in the Justice Department's 1984 Merger Guidelines appears justified in light of the evidence from this study that efficiency forces can be a powerful cause of horizontal mergers" (p. 34).

Manne (1965) argued that, "A fundamental premise underlying the market for corporate control is the existence of a high positive correlation between corporate managerial efficiency and the market price of shares of that company" (p. 300). Manne presented the reason as:

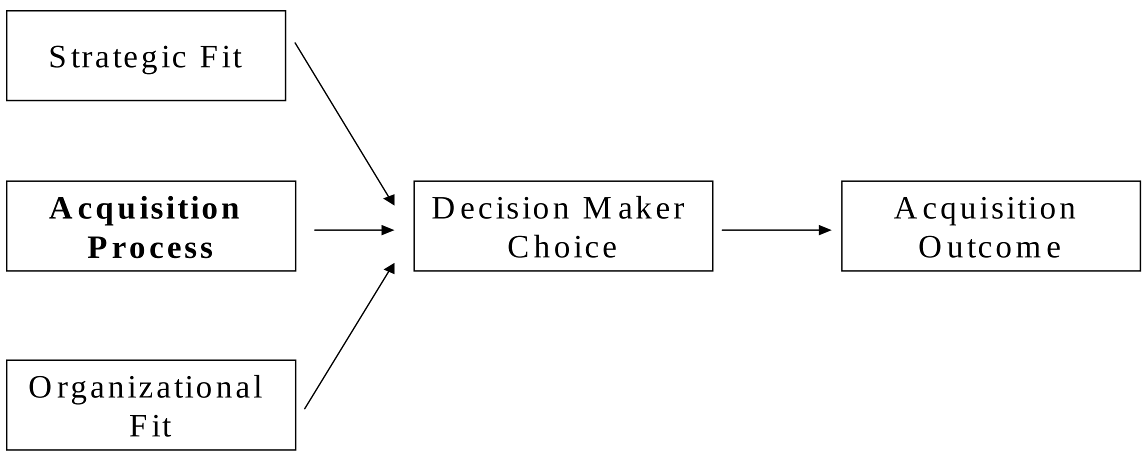
> "The claim of a positive correlation between managerial efficiency and the market price of shares would seem at first blush to raise an empirical question. In fact, however, the concept of corporate managerial efficiency, with its overtones of an entrepreneurial function, is one for which there are no objective standards. But there are compelling reasons, apart from empirical data, for believing that this correlation exists. Insiders, those who have the most reliable information about corporate affairs, are strongly motivated financially to perform a kind of arbitrage function for their company's stock. That is, given their sense of what constitutes efficient management, they will cause share prices to rise or decline in accordance with that standard. The contention is often made that stock-market prices are not accurate gauges, since far more trades take place without reliable information than with it. But there is reason to believe that intelligence rather than ignorance ultimately determines the course of individual share prices. Stock-market decisions tend to be of the one-out-of-two-alternatives variety, such as buy or not buy, hold or sell, or put or call. To the extent that decisions on these questions are made by shareholders or potential shareholders operating without reliable information, over a period of time the decisions will tend to be randomly distributed and the effect will therefore be neutral. Decisions made by those with a higher degree of certainty will to that extent not meet a canceling effect since they will not be made on a random basis. Over some period of time it would seem that the average market price of a company's shares must be "correct" one" (p. 300)

Influences and Problems in the Overall Acquisition Processes

The acquisition process involves a wide variety of information, tasks, and manpower in analyzing, synthesizing, and evaluating both conceptual and technical details. If we can identify the effective acquisition process that leads to achieving the anticipated synergistic benefits, it may be possible to argue that the merits of a study will be substantial. This section will focus on previous studies on influential factors and problems in the overall acquisition management process and then impact on post-acquisition performance.

Traditional corporate acquisition scholars mostly adapted a choice perspective or a rational decision model in conducting their research. Some researchers pointed out that the choice perspective may not provide a comprehensive view of the acquisition processes and outcomes (Jensen & Ruback, 1983; Lubatkin, 1983). Most of the previous research based upon a rational choice perspective has had two key points: strategic fit, and organizational fit, that seemingly have a narrowly focused viewpoint. These two popular "fit" models will be discussed later in the section on the pre-acquisition management process. However, Jemison & Sitkin (19861) argued that the acquisition process itself has had the most important role in determining acquisition activities and outcomes, and the conventional choice perspective should be supplemented with a process perspective (See Figure 3). Furthermore, the authors argued that the acquisition process perspective has not been studied previously as a crucial determinant of acquisition activities and outcomes.

Jemison & Sitkin (19861) stated that strategic fit or organizational fit models were focused on "successful and unsuccessful practices, these perspective approaches are a source of interesting research ideas. However, applied research can sometimes miss key issues that theoretical approaches reveal. Such is the case, the present authors contend, in acquisition research where clues to understanding acquisition outcomes may be discovered more readily in a variety of theories that direct to the underlying process-driven impediments to effective acquisitions" (p. 146).



Note: The process perspective emphasizes that the acquisition process in another factor, in addition to strategic fit and organizational fit, that affects acquisition outcomes

From Jemison & Sitkin (1986[1])

Figure 3. A Process Perspective on Corporate Acquisitions

Jemison & Sitkin (1986[1]) proposed three assumptions for an integrated viewpoint among three critical dimensions, which are comprised of strategic, organizational, and process factors, in the acquisition management process for related business acquisitions, including; 1) appropriate analysis of strategic fit is a critical factor for successful acquisitions; 2) related business acquisitions inherently require more accurate analysis in organizational fit; and 3) acquiring companies' managers frequently ignore a variety of impediments in the process of analyzing, negotiating, and acquiring the target firms. The authors identified four impediments that seriously affect the overall acquisition process in determining overall acquisition success for related business acquisitions, which are primarily focused on achieving the anticipated operating synergies between the acquiring company and the target company. According to Jemison & Sitkin (1986[1]), four impediments to the acquisition process are: 1) Activity segmentation – "The technical complexity of the activities surrounding an acquisition and the traditional roles of the participants lead to task segmentation" (p. 148); 2) Escalating momentum – "The forces that stimulate momentum in the acquisition process are stronger than those forces that retard its momentum" (p. 151); 3) Exceptional ambiguity – "The presence and use of ambiguity during the negotiation phase of an acquisition are often quite purposeful" (p. 156); and 4) Management system misapplication – "The parent's desire to help the new subsidiary and their confidence about their own capabilities often lead to misapplication of management systems which reduces the chances for the acquisition's ultimate success as a subunit of the parent firm" (p. 159).

Corporate acquisitions frequently produced a disappointing result for the acquiring companies' shareholders' wealth. After an exhaustive study, through observing the actual field performance of hundreds of businesses, Young (1981) found that "the underscored bottom line of this matter suggests that the undesirable consequences of acquisition/merger failure can only be reconciled by management (p. 605). Young (1981) argued that management may manage the incremental variables better through paying attention to all steps of an acquisition, therefore manipulating all related events in reference to each application to business and the demands of the acquisition. Young (1981) further stated that:

> "As a consequence, emphasis on timing and communicative coordination has been observed to be a most critical concern. Further, most successful acquisition/mergers are coordinated by one competent individual who centrally controls and directs the total effort" (p. 606).

Young (1981) also identified a wide variety of control points, which affect the overall acquisition management process. The author argued that when control points are unidentified, it causes unguided acquisition programs, and the relative effects of random chance deter achieving the high potential of anticipated acquisition synergies. In terms of methodological issues, Young (1981) adopted ten decision factors that imply the interdependent aspects of an acquisition transaction. Young (1981) further stated that:

> "The relative success of any buyer or seller can be measured by the degree in which the problem elements are realized, the depth in which they are suited, and the application of results obtained. Due to the singular nature of the individual decisions and how they relate to each transaction, it is better to identify decisions by a series of steps or elemental categories" (p. 610).

Young's (1981) ten decision factors are described in Table 9. Due to the logically progressive nature of describing the events within the mechanism of the transaction, the author indicated that these ten decision factors were considered. Most importantly, the author stated that "Knowing what to do at the appointed time can make the difference between achieving success or failure" (p. 611). Since acquisition includes personal, economic, and management decisions which resist easy and superficial comment, the author pointed out that the ten decision components should be collectively addressed in proper perspective and sequence.

Table 9. Ten Decision Factors in Acquisition Management Process

Decision Factor	Definition
Motivation	A decision to attempt the sale or purchase of a business
Contact	A decision as to the method of determining a buyer/seller of a business with specified characteristics
Information	A decision on the information needed to purchase/sell a business
Sources	A decision on the logistics and cost impact requirements governing the development of information
Analysis	A decision on the significance and reliability of obtained information
Value	A decision on what the actual worth of the business should be
Price	A decision on how much capital is to be expected for the business
Financing	A decision on the method of transacting capital (or other asset equity)
Contract	A decision on the form and content of the contractual relationship
Implementation	A decision on the mechanism to be utilized in effecting ownership transfer

[From Young, 1981]

Marks & Mirvis (1998) identified a wide variety of problems during the overall acquisition processes, as shown in Table 10. The authors further stated that, “People can never receive answers to all their questions in a combination; they can never get enough support to assuage all their anxiety. Given a critical mass of unknowns, an insatiable appetite for answers, and an overarching atmosphere of cynicism about corporate leadership, the best that senior management can do is make a solid case for the combination, plan it carefully, put the companies together sensibly, and reach out to people to get them involved and give them support. People’s faith in leadership and confidence in the future grow when they see the combination being well managed. Their self-confidence is boosted, too, as their ability to cope with stress and adapt to change increases and as they are involved in building the new; generating ideas, working proactively with counterparts and customers, and living out the values and behavior of the desired outcome” (p. 275). Based upon their extensive experience in acquisitions, Marks & Mirvis (1998) recommended five key dimensions for focusing top management’s attention and resources over the process of an acquisition, as shown in Table 11.

Table 10. Problems in the Acquisition Process

Phase	Problem
Pre-Combination	• Unclear business strategy • Weak core business • Poor combination strategy • Pressure to do a deal • Hurried due diligence • Overvalued targets and overestimated synergies, prospects, and returns
Combination	• Integration seen as a distraction from "real work" • Misunderstood value-added and critical success factors • Psychological effects denied or ignored • Culture clash denied or ignored
Post-Combination	• Renewed merger syndrome • Rushed implementation • Insufficient resources deployed • Unanticipated implementation obstacles • Coordination snags • Inattention to team building • Culture by default, not by design • Unintended impact on employee attitudes and hence business performance • Missed opportunities for organizational enhancement

[From Marks & Mirvis, 1998]

Table 11. Managing the Five Dimensions of a Combination

	Precombination	Combination	Postcombination
Strategy	Clarify strategy, rationale, and search criteria	Develop and follow vision and CSFs	Maintain executive oversight
Organization	Conduct through screening and due diligence	Study opportunities to build a new and better organization	Align organizations, policies, practices, and groups
People	Prepare people psychologically	Get the right people in place and onsite	Regroup individuals and build teams
Culture	Respect the precombination cultures	Manage culture clash and culture building	Reinforce the desired culture
Transition Management	Know where you want to go … and what it takes to get there	Create and staff a transition structure to execute an integration program	Learn from this combination so as to better manage future ones

[From Marks & Mirvis, 1998]

The Pre- and Post-Acquisition Management

This section will focus on previous studies concerning key factors and problems in both pre- and post-acquisition management processes and their impacts on post-acquisition performance. This section will be divided into two parts, including: 1) The pre-acquisition management process; and 2) The post-acquisition management process.

The Pre-Acquisition Management Process

Pre-acquisition management is almost equivalent to the formulation of strategy. If the acquirers do not identify and prepare the details of the acquisition plan and a wide variety of specific processes, the anticipated synergistic benefits will be in jeopardy. Marks & Mirvis (1998) identified three key areas of the pre-acquisition management phase: strategic, operational, and psychological. The authors stated the details as:

> "The strategic challenges concern key analyses that clarify and bring into focus the sources of synergy in a combination. The operational challenges involve "reality testing" potential synergies in light of the two sides' structures and cultures, and establishing the desired relationship between the two companies. The psychological challenges cover the actions required to understand the mind-sets people bring with them initially and develop over the course of a combination. This means raising people's awareness of and capacities to respond to the normal and to-be-expected stresses and strains of living through a combination" (p. 55).

Marks & Mirvis (1998) further pointed out the four aspects continually assessed and negotiated by the acquisition task forces for a potential acquisition, as shown in Table 12.

Table 12. Four Aspects of Pre-Acquisition Management

Aspect	Description
Purpose	Define the strategic intent of the lead company or both parties, and detail the business case supporting the deal
Partner	Develop clear and cogent criteria for use in the research for a partner, assess the two companies' organizational and cultural fit, and conduct due diligence in a manner that builds a deep and accurate understanding of what might be merged, aligned, or kept separate
Parameters	Establish the relationship between the parties, and delineate the desired end state of the combined organization
People	Understand and contend with the first phases of the merger syndrome and the distinct psychological patterns of perceived winners or losers in the combination

[From Marks & Mirvis, 1998]

There are some other previous studies regarding the acquisition process. Table 13. summarizes those studies' results.

Table 13. Summary of Previous Acquisition Process Studies

Author	Content of the Acquisition Process
Rappaport (1998)	1. Competitive analysis: Identify synergies between the acquirer's businesses and potential other businesses' areas that it may wish to penetrate, through identifying opportunities of cost savings or achieving differentiation. 2. Search and screen: Develop a list of potential targets, and screen candidates based upon established evaluation criteria. 3. Strategy development: Develop synergy-gaining implementation plan, through developing operational strategies to explore synergies systematically. 4. Financial evaluation: Identify or determine maximum acquisition price, primary risks involved, and the acquisition's impacts on cash flow and balance sheet. 5. Negotiation: Eliminate human nature-oriented problems (i.e., ego, emotion, etc); emphasize interests, not positions; develop options for mutual benefit; and use objective criteria.
Copeland, Koller, & Murrin (1994)	1. Manage pre-acquisition phase: • Organize acquisition • Evaluate own strength and weakness • Identify value-adding method (reinforce core business, identify opportunities of scale economies, and identify benefits from technology or skills transfer 2. Screen targets: • Establish knockout criteria • Determine leverage of investment banks • Prioritize opportunities • Search various types of business firms (i.e., public or private firms) 3. Value remaining targets: • Acknowledge how to recoup the acquisition premium • Make sure of synergies • Determine restructuring strategy • Determine of financial engineering opportunities 4. Negotiation: • Determine maximum acquisition price and stick to it • Know value of potential competing bidders • Develop negotiation strategy • Conduct due diligence 5. Manage post-acquisition integration • Quick movement • Careful process management

A. INFORMATION

The success of acquisition activities depends on how an acquiree's value and competitive resources are utilized in order to accomplish the expected synergistic benefits for a combined firm. In her seminal book, The Theory of the Growth of the Firm, Penrose (1959) stated that:

> "Hence acquisition can be used as a means of obtaining the productive services and knowledge that are necessary for a firm to establish itself in a new field, and the addition of new managerial and technical services to the firm's internal supply of productive services is often far more important than the elimination of competition

and the reduction of the costs of entry" (p. 128).

Barney (1988) argued that mode in acquisition relatedness is not the single most important factor in determining whether or not an acquisition is successful. Barney studied sources of abnormal returns for the acquiring companies, and suggested two key sources of abnormal returns in acquisition activities. The first of Barney's sources of abnormal returns is the acquirer's capacity to avoid high bidding prices. The acquirer's acumen in identifying the realizable value from strategic relatedness between a firm and a target will lead to a high likelihood of abnormal returns. The second source of abnormal returns is the capability of the acquiring firm to identify and capture the potential benefits of strategic relatedness among other bidding companies and targets. Barney (1988) concluded that, "in order to obtain expected above-normal returns from acquisitions, firms must complete acquisitions only imperfectly competitive markets for corporate control" (p. 78).

Key Success Factors. Drucker (1981) suggested five rules for profitable acquisitions. They are: (1) acquire a target with similar technology or markets or production processes to those of the acquirer; (2) calculate the potential improvements, in addition to money, created by the acquiring firm; (3) full observation of target's products, markets, and customers; (4) help the acquired company by providing new top management within a year; and (5) promote a substantial number of managers for both the acquiring company and the acquired company. However, every acquisition is accompanied by high risks, as Paine & Power (1984) stated, "following Drucker's rules probably does not significantly reduce these risks and following them may create long-run competitive problems" (p. 108).

Raab & Clark (1992) argued that an effectively managed human component in integration, and the seven key success factors described below, are the recipe to a success. These success factors were developed through the authors' first-hand experience, study of cases, and discussion with executives who had post-acquisition integration experiences. The seven key success factors are: (1) Recognize the magnitude and difficulty of the undertaking; (2) Develop a realistic goal for the combined firm; (3) Discover the right target; (4) Seize top management cooperation without giving away the store; (5) Plan the appropriate post-acquisition process early; (6) Move rapidly; and (7) Communication. Communication. Communication.

Anslinger & Copeland (1996) identified seven important operating principles that are affect most phases of the overall acquisition process, including: (1) Insist on innovative operating strategies; (2) Do not do the deal if you cannot find the leader; (3) Offer big incentives to top-level executives; (4) Link compensation to changes in cash flow; (5) Push the pace of change; (6) Foster dynamic relationships among owners, managers, and the board; and (7) Hire the best acquirers.

Broad involvement of key employees throughout the acquiring firm is one of the most important factors in a successful acquisition. Lack of consideration of the operational aspects is frequently mentioned by previous researchers. Active participation of operational managers and key members throughout the entire acquisition process is becoming a core ingredient of a successful acquisition outcome. Such operational side-peoples' involvement can facilitate better strategic choices by fostering a broader and more comprehensive information base, and can be a valuable contribution from those who will have to implement the decisions made during acquisition negotiations (Drucker 1981; Searby, 1969). Bernard Schwartz, chairman of the Loral Corporation, a company in the defense electronics industry, mentioned an important point, as follows (Jemison & Sitkin, 1986[2]):

> The planning is done by our operating people … so that the people who are doing the acquisition are the same ones who are going to be involved with those people in the future. I think it is the key part of making successful acquisitions. … I will not resort to outside consultants or outside analysis because I think we're the experts, and if we have to depend on outsiders, then we're in trouble in terms of how to manage the company afterwards (p. 111).

Marks & Mirvis (1998) identified some characteristics of successful acquirers' behavior during the overall acquisition process, as shown in Table 14. The authors also proposed a variety of lessons from successful combinations, as shown in Table 15.

Table 14. Differences Between Typical vs. Successful Acquirer

Phase	**Typical Emphasis**	**Successful Emphasis**
Pre-Combination	Financial	Strategic
Combination	Political	Combination Planning
Post-Combination	Damage Control	Combination Management

[From Marks & Mirvis, 1998]

Table 15. Lessons Learned from a Successful Combination

Things we did right:
• Appointed a dedicated transition manager • Formed an integration team • Speedy decisions (thus shorter disruption period) • Appointment of management team by deal closing date • Decision to expand management team during transition • Aggressive employee communications program • External consultant working with management team and key staff • Managing team driving structural integration (enhanced accountability and commitment) • People selection and outplacement process • Attention to details of major announcements, like headquarters location • Launch of postcombination vision and mission statement on one year anniversary of deal closing
Things we could have done better:
• The integration team was under-resourced (not enough people) • Speedy decision led to less analysis and some bad decisions • Committee approach to politically charged decisions like headquarters location • Better manage employee expectations (winners acting in a dominant way; losers acting in a passive way) • Not enough hands-on leadership presence • Underestimated the impact of cultural differences • Defining our expectations of staff groups and business regions to fully integrate business • Had no plan for educating ourselves on each other's products • Senior managers from lead company did not do as well as expected in overcoming culture clash • Pay more attention to field sales force • Pay more attention to undistributed sites (although they were not directly changed, they resisted cooperating with changes in other areas) • Not be so naïve as to believe what the investment bankers told us about sales synergies in the first year; underestimated disruption to business
Therefore, we would do the following differently:
• Establish a larger integration team • Manage expectations from Day 1 and give clearer directions to senior management from lead company • Make site decisions by management and not by committee • Push more aggressively for some balance between the partners in all functions • "Select the best people while achieving the best balance" • Provide cultural integration training to broader organization, not just management team

[From Marks & Mirvis, 1998]

Evaluation of Acquisition Targets. In order to be successful in acquisitions, precise evaluations of target companies are the first and foremost task for acquirers. An acquisition bid should meet appropriate needs within the acquirer's organization and, ultimately, should increase shareholders' value. Many researchers, including Salter & Weinhold (1979), have argued that acquiring firms typically overestimate the value of the target firm by underestimating the costs of realizing synergies with the target. Such miscalculation caused below normal returns for the acquirer.

According to a resource-based view of the firm, Markides & Willamson (1996) argued that acquisition relatedness must be measured as the degree of strategic assets. The authors pointed out that, “the strategy of related diversification will enhance performance only when it allows a business to obtain preferential access to strategic assets—those that are valuable, rare, imperfectly tradable, and costly to imitate. Even then, the advantage afforded by this access will eventually decay as a result of asset erosion and imitation by single-business rivals. In the long run, therefore, only accumulated competences that enable a firm to build new strategic assets more quickly and efficiently than competitors will allow it to sustain supernormal profits” (p. 363). Those strategic assets are classified into five categories, developed by Verdin & Williamson (1994): (1) customer assets (i.e., brand recognition, customer loyalty, and installed base); (2) channel assets (i.e., established channel access, distributor loyalty, and pipelinestock); (3) input assets (i.e., knowledge of imperfect factor markets, loyalty of suppliers, and financial capacity); (4) process assets (i.e., proprietary technology, product or market-specific functional experience, and organizational systems; and (5) market knowledge (i.e., accumulated information on the goals and behavior of competitors, price elasticity of demand, or market response to the business cycle).

In broad terms, there are two fundamental aspects to acquisition activities. As Kantor (1970) stated, “the tactical aspects of a merger transaction include the price negotiations, service analysis, evaluation of the company’s status in its industry or area, the determination of asset values and liabilities to be assumed, legal matters, terms of payment for the purchase, and relationships with retiring executives of the company being acquired. The strategical aspects of a merger involve the long-term relationships between the acquired company and the acquiring company” (p. 55).

According to Ernst & Young (1994), there are three components that comprise the analytical framework for M&A evaluation criteria, including: industry competitive factors, operating strategy, and target’s competitive position. These three components will determine the future acquirer’s profitability. Ernst & Young also proposed a “list of categories (that) should be helpful in developing the necessary information about a target company for the evaluation process” (p. 33). The list includes: target’s market served, types of products, customer characteristics, suppliers, operational characteristics, target’s market position, competitive behavior, market boundaries, and target’s financial performance measures. Further, Ernst & Young stated that the required actual information may vary, depending on individual circumstances.

Previous researchers in the strategic management arena identified that decisions are based upon a group of objective criteria by which strategic alternatives are assessed (Ackoff, 1981; Camillus, 1982). Park & Hitt (1997) identified 15 evaluation criteria of target firms in the acquisition decision-making process used by diversifying firms' top executives. These criteria were identified based upon a literature review and suggestions from academic experts in the strategic management arena. The evaluation criteria selected included degree of diversification, market share, annual sales, return on investment, stock price, cash flow projections, anticipated new products/services to be offered over the next five years, anticipated demand for products/services over the next five years, level of management expertise, marketing competence, manufacturing capabilities, competence in R&D, target's industry attractiveness, level of synergy with the acquirer, and bidding price. Park & Hitt conducted the study through the development of 30 hypothetical cases by asking executives about each target's attractiveness and its probability of being acquired. The authors utilized a pilot study to verify the validity of the instruments, which proved to be a viable and inclusive medium. In addition, Hitt & Tyler (1991) found that U. S. executives tend to place a lot of emphasis on synergy in their acquisition decisions.

From their banking industry acquisition study, Raab & Clark (1992) pointed out that the core of choosing the right target is to establish a selection criteria based upon an articulated strategic vision. The authors identified those criteria as; product, culture, customers, geographic focus, management expertise, possession of other resources, and anticipated benefits. Ernst &Young (1994) proposed a general information guide that needs to be collected during the target evaluation, as shown n Table 16.

Table 16. Information Guidelines for Target Evaluation

Category	**Description**
Products/Markets	• Breakdowns of volumes/margins by product lines, as a basis for determining future growth (existing and new products) • Requirements/costs for future sales and marketing • Trends for pricing/margins; future constraints/opportunities
Operations/Organization	• Cost structure components, current and expected • Key staff requirements/costs • Labor costs/expected requirements/relationships
Financial	• Capital expenditure requirements • Working capital relationships and the impact of growth • Costs that stay/grow/decline after the acquisition • Synergies that may reduce costs
Industry/Competition	• Competitor actions as they may affect pricing or unit demand • General industry trends as they may affect revenues or costs

[From Ernst & Young, 1994]

Strategic Fit and Organizational Fit. In order to achieve explicit goals from corporate acquisitions, acquirers may need to consider the "fit" between the acquirer and the target, including strategic fit and organizational fit. Jemison & Sitkin (1986[1]) defined strategic fit as "the degree to which the target firm augments or complements the parent's strategy and thus makes identifiable contributions to the financial and nonfinancial goals of the parent" (p. 146). The authors also defined organizational fit as "the match between administrative practices, cultural practices, and personnel characteristics of the target and parent firms and may directly affect how the firms can be integrated with respect to day-to-day operations once an acquisition has been made" (p. 147). Furthermore, according to Jemison & Sitkin (1986[2]), "The first emphasizes the strategic fit between the acquirer and its target and the importance of ensuring that the proposed subsidiary can contribute to the parent's strategy. The second approach stresses the need to achieve an organizational fit between the two companies by matching administrative systems, corporate cultures, or demographic characteristics. Sufficient degrees of strategic and organizational fit ought to guarantee an acquisition's success" (p. 107).

The strategic fit between the acquirer and the target is concerned with "how the distinctive competencies of the target could be combined with those of the suitor to create additional value" (Jemison & Sitkin, 1986[1]). A wide variety of involvement, especially operating managers and key staff people, can facilitate better strategic choices by fostering a broader information base and greater commitment from those who will have to implement the decisions made during the acquisition process (Drucker, 1981; Searby, 1969). The organizational fit studies dealt with such aspects as the impact of acquisitions on individual motivation and productivity (Graves, 1981; Levinson, 1973; Mace & Montgomery, 1962; Marks, 1982) and the difficulties encountered in the matching firm's or CEO's operating styles (Barrett, 1973; Costello, Kubis & Shaffer, 1963; Kitching, 1967) or management control systems (Leighton & Tod, 1969; Mace & Montgomery, 1962). Weber, Shenkar & Raveh (1996) stated that, "Management should pay at least as much attention to cultural fit during both the pre-merger search process and during the post-merger integration process as it does to finance and strategic factors. A lack of cultural fit may undermine the prospect of achieving synergy or add cost to the integration process, thus offsetting one of the main raison-d'etre of the merger" (p.1225).

B. VALUE

There is no question about the goal of acquisitions. That is, to add value to the acquiring firm and then maximize shareholders' wealth. The value of an acquisition must depend upon a feasible cash flow from operations. According to Sirower (1997), "synergy is realized when cash flows are increased (through higher revenues from increased product sales or higher prices and/or through lower costs) or when the discount rate on projected cash flows falls below what was reflected in the firm's pre-acquisition share prices" (p. 47). Synergy is a magic word in the acquisition arena. Sirower (1997) defined "synergy is the increase in performance of the combined firm over what the two firms are already expected or required to accomplish as independent firms" (p. 20). One of the fundamental concepts concerning building synergy is that the whole is better than the sum of its parts, an idea that stems from systems theory.

In general, three types of synergies can be identified. First, financial synergy, which is aimed at achieving a lower cost of capital through lowering the systematic risk of the acquirer. Second, operational synergy strives to achieve operational excellence from the combined firm's operations. Scale economies and cost saving are the primary goals of operational synergies. Third, managerial synergy attempts to enhance a target's competitive position by transferring management expertise from the bidder to the target. However, Marks & Mirvis (1998) argued that, "To get one plus one to equal three, a combination must yield more than synergies based on economy of scale and elimination of redundancy. Although financial synergies can contribute significant savings, one-time gains do not leave the organization in a position to maintain a competitive edge in the long run. Neither does a focus on cost cutting tap the full potential of a combination" (p. 5).

Kozin & Young (1994) suggested a valuation model based upon the value of core competencies. Its analytical process can be classified into three distinctive elements: (1) The valuation cash flows from the acquired firm's recognizable products and services; (2) The value, such as revenue and cost synergies, created by ownership changes of the acquired firm; and (3) The value creation initiated through cross-utilization and/or better exploitation or a combination of core competencies. Sirower (1997) identified four major elements of synergy based on considerations of premiums and competitor reactions: strategic vision, operating strategy, power and culture, and systems integration (See Table 17). Sirower further asserted that if these four cornerstones of synergy were negated by the acquirer, the acquisition premium represents a synergy trap for the acquirer at the shareholders' expense.

Table 17. The Cornerstones of Synergy

Synergy Cornerstone	**Description**
Strategic Vision	"Strategic vision is where all acquisitions begin. Management's vision of the acquisition is shared with suppliers, customers, lenders, and employees as a framework for planning, discussions, decisions, and reactions to changes. The vision must be clear to large constituent groups and adaptable to many unknown circumstances" (p. 29).
Operating Strategy	Operating strategy must satisfy, "What can be further sustained or improved along the value chains of the businesses that competitors cannot challenge, and how can competitors be attacked and disabled?" (p. 31).
Systems Integration	"Systems integration focuses on the physical integration plans that must be in place to implement the strategy (such as integration of sales forces, distribution systems, information and control systems, and R&D and marketing efforts" (p. 35).
Power & Culture	"Power and culture focuses on the reward and incentive systems and the control of information and decision processes at various levels of the organization" (p. 35).

[From Sirower, 1997]

Many acquiring firms attempt to seize synergy to compensate for their premium and to gain improved value. However, as mentioned earlier, more than 50 percent of the acquirers' lost on their investments, rather than gained value (synergy). Sirower (1997) stated some implications of synergy:

> "When executives play the acquisition game, they pay, in addition to the current market price, an up-front premium for an uncertain stream of payoffs sometime in the future. Since shareholders do not have to pay a premium to buy the shares of the target on their own, these payoffs, the synergies, must mean improvements in performance greater than those already expected by the markets. If these synergies are not achieved, the acquisition premium is merely a gift from the shareholders of the acquirer to the shareholders of the target company" (p. 19, 20).

Chatterjee (1992) investigated the sources of value in corporate acquisitions by saying that the source of value resides in the target firm. In order to gain value, the target firm must accept restructuring to change and improve its overall prosperity, otherwise it will lose value after the transaction. This assertion contends that the conventional source of acquisition, synergy itself, advocated by many previous researchers, means that "if a takeover is motivated by synergy, physical consolidation of the bidder and target assets is necessary to create value" (p. 270). Chatterjee also found that the initial takeover bid represents an indicator for hidden value in the particular industry of the target. Chatterjee (1992) argued that, "while the overall sample seemed to be midly supportive of the idea that tender offers should not be rejected, the more detailed investigation suggests that this advice is more appropriate for management who are not capable and/or willing to pursue the value creating opportunities revealed by the tender offer" (p. 281). Chatterjee (1992) proposed a framework, as shown in Figure 4, that represents the nature of value generating information at the time of the initial takeover bid, and its implications on the process by which anticipated profits (value) from the acquisition are realized. Chatterjee summarized some testable implications for the acquirer, in Figure 5, that represent expected stock price changes of targets, rivals, and acquirers during an acquisition announcement and after the acquisition attempt fails, under different classes of information about the source of value in the acquisition. The author further stated that, "Since the takeover related gains are expected to be capitalized around the time of the takeover, we would expect the stock price of a portfolio of successful bidders to be stable after the takeover announcement period irrespective of the motive behind the takeover. On the other hand the unsuccessful bidders should lose all the announcement period gains and then their stock price should stabilize" (p. 272).

	Nature of information regarding value from acquisition		
	Industry-wide Restructuring	Firm-specific Restructuring	Synergy
Value realized by: Physical consolidation of the assets of the target and bidder	Usually not needed	Usually not needed	Usually needed
Transactions in the goods and capital market	Usually available	Usually available	Usually not available

From Chattejree (1992)

Figure 4. The Relationship between the Nature of Information and Value from Acquisition

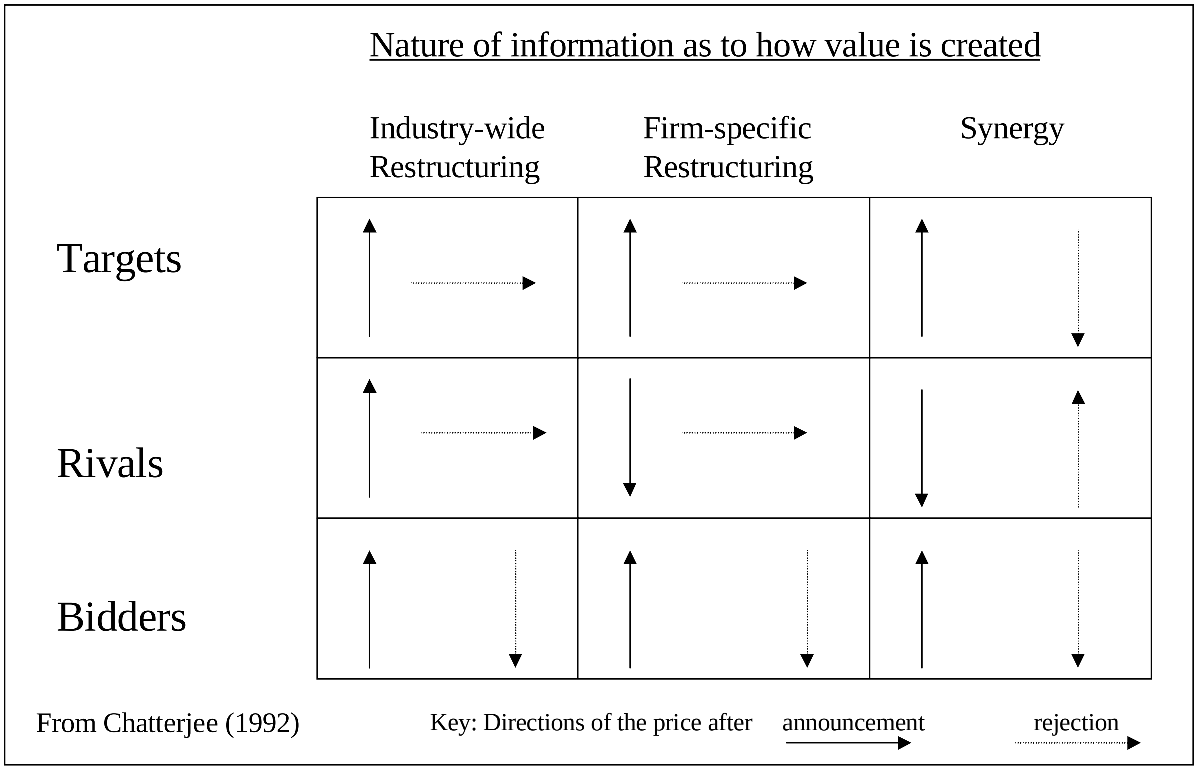


Figure 5. The Relationship between the Nature of Information and Expected Share Price Change in Acquisitions

According to Grundy (1992), there are four types of strategic values created from acquisitions: (1) Protective value (by protecting existing business); (2) Enhancing value (i.e., establishing the existing competitive position); (3) Synergistic value (i.e., by seizing joint value-chain benefits); and (4) Future opportunity value (i.e., through creating a platform, or stream of future opportunities). Grundy (1992) also suggested an 'iceberg of acquisitions investment,' by saying, "The idea of the 'iceberg' of acquisition investment implies that managers frequently under-assess their total investment requirements. Some parts of investment are highly visible, some are less visible, and others are actually invisible. Some parts are visible to experienced acquirers but invisible to the less experienced" (p. 184).

Benefits gained by service firms are not different from those that have been sought by manufacturing industry acquirers (McCann, 1996). Based upon this assumption, McCann (1996) investigated the primary strategic benefits pursued by the service sector acquirers, including transportation & travel, retailing, financial services, communications & information services, and professional services. The author identified seven benefits of service firms' acquisition as (1) increased market share, (2) increased capacity to offer new products/services, (3) improvements in brand & reputation, (4) improved efficiency in resource allocations, (5) increased scale economies, (6) enlarged asset base, and (7) acquisition of management expertise. The author attempted to discover the key benefits sought by service sector acquirers. The results are shown in the order introduced. McCann (1996) also investigated the key obstacles encountered in service sector acquisitions, and identified their order as (1) cultural differences, (2) integration of human policies and personnel problems, (3) need for significant cost cutting, (4) a lack of strategic fit, and (5) increased debt obligations.

Brand is an intangible asset, but sometimes possesses much more value than tangible assets. Parr (1993) pointed out, "the brand may be worth more to the buyer than the seller because the deal unlocks hidden values. Under accounting rules, the company that developed a brand cannot assign it a value or carry it on the balance sheet as an identifiable intangible asset. But once the brand changes hands, the buyer can value it and plug it into the balance sheet" (p. 36). Parr introduced some techniques used to calculate value of brand in dollar terms, as: (1) The cost of developing the brand; (2) The prices that comparable assets fetch in the market; and (3) The income projections that the asset can create. Parr (1993) further stated that:

> "Acquirers of brand-name companies rarely look back after paying a high price that may include an incalculable "glamour premium." The price may turn out to be a bargain, because the buyer can exploit a brand strategically while, unlike the seller-creator, value it as a recognized asset. That versatile financial ploy can generate benefits ranging from expansion of the asset base to reducing acquisition goodwill. The most popular methodology for valuing an acquired brand is the income stream approach, essentially a DCF projection of future cash flows. Alternatives, which are more difficult to use, base valuations on the cost of creating the brand or on what the brand can be sold for in the m&a market" (p. 37).

According to Rappaport (1998), to calculate the value-adding opportunities from an acquisition for the acquirer, evaluation should be classified into: (1) stand-alone value of the target; (2) the value of acquisition gains; and (3) the acquisition purchasing price. These four fundamental evaluation frameworks can be expressed as shown below (Rappaport, 1998):

- Value created by acquisition = Value of combined firm – (Stand-alone value of acquirer + Stand-alone value of target)
- Maximum admissible acquisition price = Stand-alone value of target + Value of potential synergies

- Value created for acquirer = Maximum admissible acquisition price – Actual purchase price
- Acquisition premium paid = Value of synergies

There are some popular methods used to estimate the value of firms and guide them in setting acquisition prices. Table 18 summarizes some valuation techniques' advantages and disadvantages. Among them, shareholder value analysis and value-based management models are most frequently utilized. First, one of the best-known valuation tools designed to facilitate value creation and cash flow improvement is Shareholders Value Analysis (SVA), developed by Rappaport in the 1980s. SVA is comprised of a two-step process. The first is a calculation of a discounted cash flow business valuation. A projection of future cash flow, including a residual value, is established and discounted at an appropriate rate, generally the cost of capital, to reach an indicated value. The second is that value drivers, such as growth rate and profit margins, etc., are varied systematically to prove the sensitivity of the intended business value to each value driver. Standardized SVA sensitivity analysis manipulates each value driver plus or minus 1 percent, although analysts now often use "relevant ranges" and divergent percentages for upside and downside fluctuations to mirror prevalent business actualities (Bielinski, 1993). However, Bielinski (1996) pointed out some limitations of SVA, especially in work with middle-market firms.

Second, Value Based Management (VBM), a first cousin of to SVA, was created through modifying some aspects of SVA. Unlike SVA, which employs projections of future cash flow, VBM utilizes historical cash flow. "Five years of historical cash flow are added up to arrive at a cumulative baseline cash flow number. That is in contrast to SVA's method of discounting future cash flows to reach an indicated value" (p. 34, Bielinski, 1993). Bielinski (1993) pointed out a difference between SVA and VBM as "… the traditional SVA 'value drivers' are too far removed from daily operations to be relevant for short-term or medium-term planning. Therefore, VBM utilizes drivers that are more directly linked to operations. Moreover, "VBM can be used to help get a handle on the company's performance and identify areas that can be improved under the present ownership. The exercise may lead the seller to conclude that the resulting cash flow and value benefits make the company worth keeping" (p. 37, Bielinski, 1993). Bielinski (1993) provided further details of VBM as:

"Instead of testing the sensitivity of a value based on a projection. VBM tests the sensitivity of the historical cash flow. VBM tells the executive how much more or less cash flow would be in the bank today if certain events had occurred differently or if the company had operated differently in the past five years. …. Value Based Management (VBM) represents one of the latest advancements in Discount Cash Flow (DCF) modeling that is available to acquirers. VBM centers on what specific steps can be taken operationally and strategically to add value to a target after the deal is signed. It is based on the target's historical performance, rather than projections, and cash flow how to record might have been changed had managerial decisions and operating environments been different. Sensitivity analysis of past results offer clues to what can be done in the future and which value drivers – e.g., sales growth, profit margins, productivity, etc. – should receive the most attention to achieve the optimal rewards. Additionally, the VBM technique allows the analyst to figure key decision-making trade-offs, since attention to one driver may generate negative effects on others or two or more drivers may have to be varied in concert to produce the best results" (P. 34).

McGillivry & McGillivray (1995) argued that, "To get a handle on real value, acquirers should tailor DCF forecasts to recognize that constant growth is an unrealistic expectation" (p. 37). The authors recommended a planning scenario incorporated with a DCF analysis as:

"If DCF-calculated terminal value represents a huge part of a purchase price, it is too important to be left to a constant growth formula. Linear or constant growth rarely develops in any measure of postacquisition performance because of myriad forces that come and go to vary results over time. The long-range horizon necessarily used to calculate terminal value therefore should incorporate all of these dynamics, especially in industries that are being shaken up constantly by technological and other changes. Scenario planning, which develops a series of alternate outcomes by taking account of a wide variety of future developments and tracing their effects on performance, is a modern response to the problem of forecasting so far ahead. Everything from competitor responses to technical advances can be incorporated in the model to generate the various outlooks. The exercise not only gives the acquirer more insight on the purchase but imposes discipline for future operations" (p. 38).

Table 18. Advantages and Disadvantages of Acquisition Valuation Techniques

Method	Advantages	Disadvantages
Discounted cash flow	• Provides a method to model expected performance and to understand sensitivities • Aids understanding of performance, cash flow, and balance sheet relationships	• May not reflect the reality of pricing trends in the markets • Methodology may be cumbersome and may involve "soft" numbers relative to residual values
Comparable transactions	• Provides a comparison with actual acquisitions-what other people are paying • Reveals who other buyers are and may offer insights into potential competitive bidders	• Transaction data may be incomplete; the most similar deals may not be published; the published deals may not be similar; every deal is unique
Comparable companies	• Provides a benchmark of how the public markets view particular industries	• May ignore the reality of expected future performance
Adjusted book value/liquidation analysis	• May be most relevant if a business is being acquired for its underlying assets as opposed to going-concern value	• May not reflect economic value of the business, especially if the target generates strong earnings

[From Ernst & Young, 1994]

C. PRICE

The determination of acquisition price is a complex and difficult task for all the acquirers. Barnes (1996) stated that, "Determining the largest part of most purchase prices requires complete understanding of the target's competitive position in its market" (p. 24). Barnes further stated that:

> "At a time when strategic acquisitions predominate, many acquirers are shooting themselves in the foot by doing a slipshod or arbitrary job of calculating terminal values in discounted cash flow analysis. Not only is the terminal value usually the largest component of a purchase prices but a major barometer of whether a deal will fit the classic purpose of a strategic acquisition to create value over a long period of time. The key to determining an appropriate price based on the target's long-range prospects is gauging its competitive position in its product or service market and whether that power and attendant financial returns can be sustained over the long haul. Based on that real-world understanding, an acquirer can apply its analytical results to pricing through a series of formulas that incorporate projected growth, costs of capital, and new investment requirement" (p. 25).

One of the distinctive characteristics of acquisition investments compared to other internal growth investments is that acquisitions usually should pay the premium over the target's current market value. Premiums have averaged between 40 and 50 percent in the first half of the 1990s. Sirower (1997) stated that, "Like a major R&D project or plant expansion, acquisitions are a capital budgeting decision. Stripped to the essentials, an acquisition is a purchase of assets and technologies. But acquirers often pay a premium over the stand-alone market value of these assets and technologies" (p. 4). Sirower (1997) found that the higher the acquisition premium paid, the higher the value lost. According to Rappaport (1998), to create value from acquisitions, the acquirers should consider that present value of anticipated synergies must be greater than the premium paid. That is, Premium paid = Value of synergies. Acquiring firms must realize that they are paying certain substantial amount of money right away for the uncertain cash flows that will be generated from target firms' operations. Rappaport (1998) further stated that:

> "More than a few of the recent acquisitions will fail to create value for the acquirer's shareholders. After all, shareholder value creation depends not on pre-merger market valuation of the target company but on the actual acquisition price the acquiring company pays compared with the selling company's cash-flow contribution to the combined company. Only a limited supply of acquisition candidates is available at the price that enables the acquirer to earn acceptable economic return on investment. A well-conceived evaluation program that minimizes the risk of buying an economically unattractive company or paying too much for an attractive one is particularly important in today's market. The premiums that must be paid by a successful bidder call for more careful analysis by buyers than ever before" (p. 135).

According to Mercer Management Consulting (Cited in Smith & Hershman, 1997), the strategy-driven acquisitions of the 1990s outperform the financially driven deals of the 1980s. However, the post-acquisition performance improvement in the 1990s is not explained by price. In fact, acquisition premiums have been higher than in the 1990s on major acquisition deals than they were in the 1980s. Smith & Hershman (1997) concluded that, "there is little correlation between price and premium and whether the deal creates value" (p. 39).

Abate (1993) argued that, "benchmarking should be used to determine what probable competitors are likely to pay for the same target, thus allowing a bidder to develop a price that both generates value and pre-empts the field" (p. 24). The author emphasized some crucial points in the benchmarking process as: (1) Identify the group of potential competing bidders; (2) Execute buy-side discounted cash flow analyses for your own company and each potential bidder; and (3) Perform comparable exercises based upon various market multiples. Abate (1993) suggested the following in calculating purchase price:

> "Putting yourself in the other guy's shoes is the essence of rational acquisition pricing. A rational price is the minimum a bidder must pay to beat out competing contenders for a target and still realize value from the deal. By benchmarking against the field, a savvy acquirer has a chance to carry off the prize without overpaying. How does benchmarking work? In brief, it starts by identifying a "peer" group of likely companies that can gain strategic and synergistic values from the target. The process then moves on to size up the optimum bid for each by running its key value drivers through a discounted cash flow (DCF) model. The company that knows its own industry or analogous fields should be able to adjust the competitor's value drivers in the DCF work-ups" (p. 25).

Morris (1994) pointed out “One of the most perilous mistakes can be an incorrect calculation or view of ‘terminal value’ – the all-important but often misunderstood final product of DCF analysis. Since terminal, or residual, value frequently comprises a huge portion – in some cases all – of the acquisition value, a miscalculation can suggest a wrong price and nullify intended value creation even before the deal is completed” (p. 24). Rather, the author suggested an alternative as:

> “By now must acquirers using discount cash flow (DCF) analysis to price and value targets feel pretty good about projecting free cash flows for an initial forecasting period – anywhere from three to 10 years after a deal closes. They are less comfortable about the cash generated later, which is the key contributor to the terminal value of the deal. That can be an Achilles’ heel in the entire process because terminal, or residual, value often comprises the bulk of the purchase price, and for high-growth, cash cow targets requiring hefty investments, sometimes all of the payout. Value-driven, strategic buyers trying to avoid overpayments based on arbitrary or imperfect terminal values are opting for the perpetuity DCF model. It assumes that cash will be generated at a constant rate after the forecasting horizon period. That allows the buyer to continue reaping value should the initial growth slow, to avoid use of unsustainable long-term growth rates, to devise value-creating strategies down the road, and to set pricing accordingly” (p. 25).

D. APPROACH

After a thorough review of the theoretical and empirical literature regarding sources of shareholder wealth creation for both the bidder and the target companies in acquisition activities, Datta, Pinches & Narayanan (1992) identified several key factors which may explain differences in value creation, including: (1) the number of bidders; (2) the bidder’s acquisition approach (i.e., merger vs. tender offer); (3) the method of payment (i.e., cash vs. stock); (4) the type of acquisition (i.e., related vs. unrelated acquisition); and (5) regulatory changes (i.e., the 1968 Williams Amendment and the 1969 tax reform). Table 19 summarizes the overall results of a Datta et al (1992) study.

Table 19. Direction of Influence of Factors on Shareholder Wealth Creation

	Bidders		**Targets**	
FACTOR	**Mechanisms**	**Direction of influence**	**Mechanisms**	**Direction of influence**
Regulatory changes in 1968 & 1969	Stimulates the market for corporate control and increases the cost of transactions.	Negative	Stimulates the market for corporate control	Positive
Number of bidders	Stimulates the market for corporate control.	Negative	Stimulate the market for corporate control	Positive
Type of acquisition approach (i.e., merger vs. tender offer)	a. Tender offers stimulate the market for corporate control and lead to an auction type process. b. Mergers provide less stimulation in the market for corporate control.	Negative Positive	a. Tender offers stimulate the market for corporate control and lead to an auction type process b. Mergers provide less stimulation in the market for corporate control	Positive Negative
Payment methods	a. Use of cash reduces time required to complete transactions and gains, if any, are not shared after the transaction with target shareholders. b. Use of stock viewed negatively by the capital market; may result in wealth transfer to bondholders.	Positive Negative	a. Cash transactions require additional premium to compensate for immediate tax consequences. b. Use of stock viewed negatively by the capital market; may result in wealth transfer to bondholders.	Positive Negative
Type of acquisition (i.e., related vs. unrelated)	Economics and transfer of core skills in related (i.e., unrelated) mergers vs. cheaper capital, lower bankruptcy probability and increased market value of debt in unrelated mergers.	Positive or uncertain	Value, if any, of relatedness primarily captured by targets.	Positive or uncertain

[From: Datta et al., 1992]

Mode of Acquisition and Payment Method. Jensen & Ruback (1983) stated that, "Mergers are negotiated directly with target's managers and approved by the target's board of directors before going to a vote of target shareholders for approval. Tender offers are offers to buy shares made directly to target shareholders who decide individually whether to tender their shares for sale to the bidding firm" (p. 7). Jensen & Ruback (1983) found that announcement period returns are higher for acquiring firms in tender offers than in mergers. According to Ikenberry, Lakonishok & Vermaelen (1995) found that cash tender offers earn higher, by an average of 12 percent, than stock offers. Loughran & Vijh (1997) mentioned a possible explanation of this result as, “It is possible that some of the excess returns earned by cash tender offers may be the result of investors underestimating the possible gains from disciplinary action associated with tender offers, such as the appointment of new managers” (p. 1768). Moreover, Sirower (1997) found that market-adjusted gains from cash offers were consistently higher than stock offer acquisitions.

Through the thorough investigation of 947 acquisition transactions from 1970 to 1989 by a 5-year period post-acquisition performance, Loughran & Vijh (1997) found a relationship among the post-acquisition return, the mode of acquisition, and the method of payment. The authors showed that, on average, acquiring firms that used stock mergers gained significantly negative abnormal returns of – 25 percent, whereas acquiring firms that utilized cash tender offers earned significantly more positive abnormal returns, of 61.7 percent. This result proved the previously, often cited hypotheses: (1) the post-acquisition value creations are higher for tender offers because of the replacement of the target’s inferior management; (2) the acquiring firms tend to choose stock offers when their stock is overvalued and cash offers when their stock is undervalued (Loughran & Vijh, 1997). Further, Lowenstein (1997) argued that, “It’s easier to realize gains by removing poor managers, as in hostile deals, than by pursuing the supposed synergies envisioned by friendly combiners,” and “acquirers who use stock tend to be those with overvalued shares—thus, the premium they confer is illusory. It takes more conviction to spend hard cash, as it does to launch a hostile bid. That is why such deals work better.”

In organizing an acquisition plan, the acquirer should determine which payment medium is appropriate to successfully take over the target firm. The acquiring company must choose the exchange medium among cash, debt, stock, or some combination. Previous empirical studies’ results are mixed. Some studies found that acquirers’ abnormal returns are lower in stock offers relative to cash offers (Travlos, 1987; Wansely, Lane & Yang (1987); Franks, Harris & Mayer, 1988).

However, Huang & Walking (1987) found higher abnormal returns to the target firm in cash offers. Moreover, Eckbo, Giammarino, and Heinkel (1988) investigated the effect of the combination of cash and stock offers on the acquiring firms’ abnormal stock returns. This combination provided a signal which uniquely relates the acquirer's private information about its own value and the value of the target, including anticipated synergistic benefits.

Fishman (1989) argued that, "A key difference between a cash offer and a (risky) securities offer is that a security's value depends on the profitability of the acquisition, while the value of cash does not" (p. 41). Fishman pointed out that the acquirer has private information on the benefits of the takeover, and thus on the value of the equity offers, whereas no party owns private information on the value of cash, all acquirers adopted cash offer. Fishman (1989) further stated that:

> "A model of preemptive bidding is developed. In equilibrium, securities are offered by lower valuing bidders and cash by higher valuing bidders. The advantage of a securities offer is its ability to induce an efficient accept/reject decision on the offer. The advantage of a cash offer is that, in equilibrium, it serves to preempt potential competition by signaling a high valuation" (p. 42).

Fishman (1989) suggested that, based on his preemptive bidding model, a target company's executives were inclined to reject a securities offer as compared to a cash offer, because a securities offer implied that the acquisition bid would not be profitable. In sum, Fishman (1989) argued that cash offers are preferred to stock offers as a means to signal high valuation and avoid competition for takeovers, when the fixed costs of gathering information about the target are high.

Hansen (1987) stated that if acquirers have private information that their equity is relatively undervalued, they tend to offer cash. However, this cash offer indicates high valuation for the target company, because the acquirers want to achieve preemptive bidding benefits. Along with the information asymmetries, Myers & Majluf (1984) argued that if the acquiring firm's management possesses superior information to that of outside investors about the value of their firm, managers will tend to prefer stock financing for an acquisition when they believe that their stock is overvalued, and vice versa. However, investors know this, and then downgrade the value of acquirers who issue new equity. In contrast, when the target firm's shareholders have superior information to that of outsiders about the value of their firm prior to acquisition, stock offers tend to be highly preferred to cash offers than when they (target) believe that their worth is undervalued (Hansen, 1984; 1987). In this case, the target firm's stockholders tend to prefer to maintain an equity position in the combined firm in order to participate in the gains from the post-acquisition revaluation.

There is a particular relationship between acquisition financing and the acquiring firm's ownership structure (corporate control). Harris & Rasiv (1988) proposed that financing preferences are based upon management's incentive to keep control over the company. According to the authors, manager-owners prefer to offer debt in order to solidity their control over the company. Amihud, Lev & Travlos (1990) suggested that a firm's capital structure policies may be related and initiated by corporate control considerations. Moreover, Amihud, Lev & Travlos (1990) found that, "the higher the managerial ownership fraction of the acquiring company the larger the probability of the acquisition being financed by cash rather than by a stock exchange offer. These findings can also be interpreted based on an asymmetry of information between corporate insiders and uninformed outside investors. If insiders hold a substantial quantity of their company's share because they believe them to be undervalued, they will be less willing to issue new stock to finance acquisitions" (p. 614). However, Martin (1996) found that there is no positive relationship between the acquiring firm's management ownership and the probability of stock financing.

In terms of the tax effects on corporate acquisitions, a cash offer creates an immediate liability for capital gains tax for the target firm stockholders, whereas an equity offer delays a tax payment obligation until the new shares are sold (Amihud, Lev & Travlos, 1990). Previous empirical studies have shown that there is no consistent relationship between the payment method and the various tax motives. For example, Nelton (1986) found no clear relationship between the tax effects of target stockholders and the mode of acquisition financing. Carlton, Guilkey, Harris & Stewart (1983) reported that, "lower dividend payout ratios and lower market-to-book ratios increase the probability of being acquired in a cash takeover relative to being acquired in an exchange of securities" (p. 825). Moreover, Auerbach & Reishus (1988) studied the three distinctive measures for the potential tax advantages of the write-up of target assets, and further stated that, "none of these were statistically significant or important in explaining the form of payment" (p. 341).

Myers (1977) argued that acquirers whose value depends more upon growth options must choose the equity option rather than debt. Martin (1996) investigated the motives underlying the mode of payment in corporate acquisitions, and found that the higher the acquiring firm's potential, the more likely the acquirer to use a stock offer to execute an acquisition. Among various influences on determining the method of payment, such as characteristics of the acquiring and the target firms, and the impacts of environment in which the acquisition takes place, Martin (1996) found two most influential characteristics in selecting the mode of payment, through investigating 846 corporate acquisitions from the period 1978 to 1988: mode of acquisition, and the acquirer's potential investment opportunities. Martin further stated that tender offers inclined to use cash offers because they are faster to consummate than mergers.

However, Titman & Wessels (1988) found that debt rations are not related to a firm's anticipated growth. Moreover, Bradley, Jarrell, and Kim (1984) pointed out a statistically significant negative relationship between growth potential and financial leverage.

As a summary, Loughran & Vijh (1997) stated the relationship among post-acquisition performance, payment method, and mode of acquisition as:

> "Despite significant evidence in favor of the asymmetric information hypothesis in the context of stock issues and repurchases, we would emphasize that this is not the only plausible explanation of our results related to the form of payment. First, the form of payment is partly endogenous to the mode of acquisition, which may be the real driving force behind the results. Second, stock acquirers tend to be growth firms, hence it is possible that both the managers and the market were overly optimistic about the firm's growth potential. Third, the positive excess returns of cash acquirers are confined to cash tender offers and are negative but insignificant for cash mergers and ambiguous cases" (p. 1775).

Relative Size of the Acquisition. One problem with previous studies dealing with acquisition performance is that they do not adjust appropriately according to the size of the firm. Dimson & Marsh (1986) pointed out that an adjustment for firm size is crucial in studies of long-term performance. Agrawal, Jaffe & Mandelker (1992) stated that, "The acquisition of a relatively large target is likely to be a more important economic event for the acquirer than is the acquisition of a relatively small target. Thus, if the post-merger underperformance reflects the impacts of the merger, underperformance should be greater when the target is relatively large" (p. 1618). Shelton (1988) found a significant positive relationship for the presence of other acquirers and the relative size of the target firm. This positive relationship between the size of a target firm relative to the acquiring firm and post-acquisition performance is supported by many other previous studies (Kitching, 1967, Waldman, 1983; Biggadike, 1979). In contrast, from the empirical evidence Agrawal, Jaffe & Mandelker (1992) found that there is no relationship between the acquirer's post-acquisition performance and the relative size of the target. Kuehn (1975), Wilson (1976), and Kusewitt (1985) supported this negative or no relationship between size and performance.

Acquisition Experience. Fowler & Schmidt (1989) found statistically significant positive relationships with post-acquisition performance and acquirers' previous acquisition experience. That is, the number of other acquisitions made in the four years prior to the specific acquisition. Moreover, Lubatkin (1983) suggested that the acquirers with previous acquisition experience may become more adept at necessary organizational changes and may therefore avoid various problems. In contrast, Kusewitt (1985) found a significant negative relationship between the number of acquisitions and post-acquisition performance. Newbould, Stray & Wilson (1976), Lubatkin (1982), De Noble, Castaldi & Monahan (1987) found no relationship between prior acquisition experience and post-acquisition performance.

Multiple Bidders. When there is more than one acquisition bidder for one target firm, there is an increase in the level of competition, resulting in a negative impact on the winning firm's post-acquisition performance. On the other hand, acquired firms' shareholders are likely to gain additional value when there are multiple bids (Datta et al., 1992). In the most extreme case, the competing acquirers end up raising the acquisition price up until the anticipated benefit is a zero net present value, or even a negative investment for acquiring firms (Barney, 1988; Roll, 1982; Ruback, 1982). Datta et al (1992) investigated empirical evidence on this topic and found that number of bidders have a negative impact on acquiring firms, whereas acquired firms have a positive impact on their shareholders' wealth. Fowler & Schmidt (1997) found a strong negative relationship between acquiring firms' post-acquisition and contested tender offers.

Negotiation Strategy. A smooth negotiation process cannot be ignored or undermined by successful acquirers. It is important to obtain the accurate information necessary to determine the acquisition price and other key points. Based upon precise assessment about potential synergistic benefits, the acquiring firm can finalize the final acquisition decision. In general, price negotiation is the primary consideration in the negotiation stage. The terms and conditions that provide economic benefits impose either advantages or disadvantages for one side, and vice versa. "A second, sometimes equally important, consideration in negotiating acquisition agreements is the preservation of the attractive nonfinancial characteristics of the company being acquired. These may include patents, trademarks, processes, or other proprietary assets. Most often, however, an acquirer should focus on the best way to assure the continuing services of key employees of the acquired company" (Ernst & Young, 1994). Henderson (1989) emphasized the importance of the negotiation process as:

> “The negotiation process provides an invaluable opportunity for each side’s management to assess the other. How well is each side prepared? How are the questions formulated? How long does it take to get responses to requests? Is the information available to answer operating questions? Are the systems formalized? The process should adopt a positive tone in which mutual benefit is sought. The purchaser should be forthright in its concerns about integration and seek the vendor’s input on how to resolve them. If a spirit of cooperation can not be achieved, one must question the foundations of the merger” (p. 34).

Due Diligence. Effective due diligence can lead to a deliberate acquisition strategy for the acquirer. Through the due diligence process, acquiring firms will have an invaluable opportunity to collect comprehensive information about the target’s operations before the execution of acquisition. Ernst & Young (1994) summarized due diligence as, “Due diligence is a process that, in short, involves learning as much as possible about a seller’s business, finances, and operations. The buyer needs to confirm the benefits of the acquisition and to ensure that there are no unrecorded liabilities or unidentified risks that could materially impact the business after the deal is consummated. … In general, a buyer will need to re-examine the following questions more closely: (1) Does the company really fit into the buyer’s strategic goals?; (2) Is it truly as attractive as it originally appeared, or are there potential problems that could arise in the near future?; (3) Can the buyer manage the company successfully and achieve the benefits that have been identified?; (4) Will the company’s management support the buyer’s objectives?; (5) Will the buyer be able to integrate the acquisition operationally and financially into its existing company?” (p. 17).

Henderson (1989) pointed out that, “Purchasers often make the mistake of thinking of due diligence as primarily a legal and accounting exercise and hence miss a valuable opportunity” (p. 33). Henderson further argued that the acquiring firms must be straightforward with targets during due diligence discussions, guide its post-acquisition goals by making a responsible statement and outlining how it anticipates accomplishing these goals, while attempting to avoid unrealistic expectations.

To achieve an effective post-acquisition integration process, Henderson (1989) summarized some critical factors that should be considered before closing a deal, as: (1) “To What extent will integration take place?”; (2) “Is sufficient management talent available?” (3) “What are the critical issues?”; (4) “How will momentum be created and maintained?”; (5) “What is the action plan?” (p. 34).

The Post-Acquisition Management Process

Why do so many well-developed acquisition plans end up with disappointing outcomes? If the anticipated synergistic benefits are accurate, that the acquisition is a promising medium for enhancing a combined firm's overall performance, we should ask the question of why the results of many acquisition activities end with unhappy outcomes over time, such as deteriorated post-acquisitions performance and/or even business failures. The lack of systematic and thorough attention paid to potential problems of post-acquisition integration appears to reflect the difficulty of recognizing the process itself as part of the problem (Jemison & Sitkin, 1986[1]). Therefore, the post-acquisition integration strategy should be planned from the very beginning stage of the overall acquisition management process, and should be managed incrementally. Post-acquisition integration may involve a complex and interactive mutual adjustment process between the two firms, but change is almost always one-sided, occurring primarily with the target firm (Buono & Bowditch, 1989; Datta, 1991; Hambrick & Cannella, 1993; Shanley, 1987; Shanley & Correa, 1992).

Differences in management styles, threats of layoffs, initial inequities in compensation programs, authority superimposed on the target firm, and an increase in size of the acquiring firm are administrative factors that may hurt the anticipated benefits of acquisitions (Lubatkin, 1983). Smith & Hershman (1997) investigated three factors, including acquisition price, strategic intent, and post-acquisition management, that might affect shareholder value, through examining more than 340 large acquisition transactions between 1986 and 1996. They concluded that "only post-merger management of an acquisition has really made a difference in determining the odds of value-creation in the major deals of the last decade" (p. 39). The authors considered post-acquisition management as the single most important determinant of a successful acquisition. Smith & Hershman further stated that:

> "The price of the transaction may be right. The strategy may be a brilliant plan to enhance the company's product or service offerings or to expand into new markets. But we have found that if an acquiring company does not move swiftly and decisively to integrate the two companies into a smoothly running firm after the deal is done, then it may be allowing value to slip right through its fingers" (p. 39).

Smith & Hershman (1997) proposed a framework for post-acquisition plans, which stress operations and strategies as well as people, as: (1) Rapid implementation of post-acquisition plan; (2) Capture opportunities for essential reengineering; (3) Manage combining cultures with sensitivity; (4) Concentrate particularly on primary customers; and (5) Take advantage of strategic options that delineate invisible value.

When the acquirer considers post-acquisition integration in terms of organizational structure, it is may be advantageous to analyze and synthesize the structural influence of the united company. Pablo (1994) approached post-acquisition integration problems by defining levels of integration as "the degree of post-acquisition change in an organization's technical, administrative, and cultural configuration" (p.806). Pablo (1994) further stated that:

> "Following the acquisition, some degree of interorganizational integration is necessary, but the issue of what level of integration managers choose and ultimately implement in the combined organization is critical to acquisition outcomes because under- or overintegration can result in a failure to create value, or worse yet, value destruction. The realization of potential synergies will be short circulated given an insufficient level of integration, but excessive reconfiguration can stymie the development of conditions conducive to a fruitful union, as occurs when high-performing executives depart in the context of an unpropitious postacquisition atmosphere, depriving the combined organization of much-needed resources and expertise (Candella & Hambrick, 1993; Hambrick & Candella, 1993; Walsh & Ellwood, 1991). A focus on the factors that influence an organization's postacquisition design strategy is central to understanding this fine balance, and thus, to disentangling the process of value creation" (p. 804, 805).

Pablo (1994) defined level of integration as "the degree of post-acquisition change in an organization's technical, administrative, and cultural configuration" (p. 806). There are three levels of integration: low, moderate, and high levels of integration. Pablo identified five determinants of the level of integration, including: strategic task needs, organizational task needs, multiculturalism of acquirer, compatibility of acquisition visions, and power differential. Pablo (1994) defined strategic task as "the successful sharing or exchange of the critical skills and resources that form the foundation for value creation" (p. 808). She also defined organization task as "the degree to which acquisition synergies depend on the preservation of a unique, context-specific set of organizational capabilities" (p. 808). Multiculturalism was defined as "the degree to which the management of the acquiring organization tolerated and valued a diversity of values, philosophies, and beliefs" (p. 817), and defined power differential as "the difference in size of the two organizations measured as number of employees" (p. 818). Pablo defined compatibility of acquisition visions as "the extent to which the acquirer and the acquired organization had compatible ideas about the goals each was trying to achieve through the acquisition and the means to achieve goals" (p. 818). The acquiring firm's degree of cultural diversity or multiculturalism may be considered as a predictor of the degree of post-acquisition integration (Pablo, 1994). According to Pablo (1994), the acquiring firm's competence to enforce its prosperity immediately after the takeover deal, and compatibility between the acquirer and the target firms become key factors in the post-acquisition management process.

Pablo (1994) investigated the relationships between the level of integration and potential determinants of the post-acquisition integration level, which include the five determinants discussed in the previous paragraph. The research indicates that strategic tasks need to be positively related to the level of integration chosen, while organizational tasks need to be negatively related. Pablo interpreted this gap as, "in integration design decisions, acquiring managers may be unable to balance these two requirements in a normatively appropriate way" (p. 824). With multiculturalism, it was found that it negatively related to the level of integration chosen, meaning that, as Pablo concluded, "organizations and their managers have paradigmatic beliefs about the functionality of culture for managing coordination and control in situations of organizational change and ambiguity" (p. 824). Furthermore, the power differential had a significantly negative relationship with the level of integration chosen, implying that "size differences are not perceived as a basis for power, but rather as a factor influencing management attention to an acquisition" (p. 824). In other words, a relatively small target to the acquirer may maintain its original structure because it doesn't attract a high degree of management interest, whereas a large target possesses a higher potential for gain or loss, and therefore the highest degree of integration is adopted, allowing an increased line of authority and a closer scrutiny for unforeseen problems. Finally, the compatibility of acquisition visions were negatively related to the level of integration chosen, meaning that, as Shanley (1987) proposed, the agency problems that may arise after an acquisition provoke the imposition of increased hierarchical control mechanisms by the acquirer. Pablo (1994) also concluded this result, as "a basis for political action exists because the ability to have influence by virtue of being the acquirer is a source of power in an acquisition in which there is disagreement over the acquisition's means or ends" (p. 825).

Copeland, Koller & Mullin (1994) emphasized that one of the critical success factors in the post-acquisition stage is to move rapidly. The authors further stated that, “post-merger acquisition integration must be carefully planned and implemented to avoid destroying value” (p. 435). Copeland et al (1994) proposed a framework for post-acquisition integration as shown in Table 20.

Table 20. Framework for Post-Acquisition Integration

Step	Content
1. Clarify purpose/set expectations	• Establish a transition mechanism • Manage expectations of acquired management • Reach agreement on top organizational issues • Plan and schedule first post-acquisition actions
2. Communicate, control, and plan integration	• Reassure key constituencies • Agree on a “get-acquainted” stage • Take the necessary control actions • Plan integration process
3. Develop strategy/basic structure	• Organize fact-finding task forces • Establish and test initial working hypotheses • Build a fact-based understanding of the comparative business systems and market positions of the companies • Identify opportunities for growth and enhancement of competitive advantage • Rank priorities
4. Refine organization/strategy	• Review initial strategy, including test of anticipated operating synergies • Review organizational similarities and differences • Implement strategic and operational change

[From Copeland, Koller & Mullin, 1994]

Grundy (1992) proposed several critical success factors for successful post-acquisition management: (1) No primary customers being lost during the first six months; (2) No key employees being lost within the first year; (3) Quick establishment of new terms and conditions within the first three months; (4) During the first two years after acquisition, notable improvements being made to product/service performance and penetration of new distribution channels; and (5) Target firm’s managers do not leave and set up business.

De Noble (1984) identified some key decision areas in post-acquisition integration: (1) Relationships between the acquirer and the target firms, particularly reporting and controlling procedures; (2) Integration of functional areas; (3) Roles and participation of both the acquirer and the target firm’s management in integration practices; (4) Extent of centralization/autonomy to be allowed; (5) compensation plans, employee benefits, and human resource policies; and (6) Timetable for completion of integration and for changing personnel. It is important to know not only ‘why’ acquisitions are made but also ‘how’ they are made (De Noble, Gustafson & Hergert, 1997). De Noble et al (1997) suggested a set of valuable lessons for the success of acquisitions as: (1) Concentration of sources, rather than symptoms; (2) Get active participation of line managers; (3) Effective integration of management team (i.e., ‘us’ vs ‘them’); (4) Acquisition of people, not only assets and technology; (5) Identify the hidden costs; (6) Transformation of culture; (7) Proper alignment between strategy and structure; and (8) Rapid post-acquisition integration process.

Based upon previous studies, Henderson (1989) identified factors that affect the high rate of failure in acquisitions as: (1) the gap between expectation and reality of the target’s management expertise; (2) the target management’s departure immediately after the deal; (3) the target’s business area was not familiar to the acquirer so that the acquirer was unable to monitor and control effectively; (4) due to the acquirer’s overoptimistic assessment, the anticipated operating synergies were not capitalized; (5) unforeseen problems (i.e., target industry’s downturn); (6) the acquirer did not identify the target’s critical success factors in the valuation stage; (7) lack of investigation about post-acquisition integration plans; (8) post-acquisition integration problems were not detected properly; (9) the acquirer’s lack of identification of the cultural distance of the target; (10) the difference between the acquirer and the target’s operating standards (i.e., the reporting system, the internal control system). Further, Henderson (1989) proposed a post-acquisition integration program as shown in Table 21.

Table 21. The Post-Acquisition Integration Plan

Pre-Acquisition Considerations	Transition Strategy
Proper due diligence	Pre-acquisition planning
Negotiating integrity	Open, clear, timely communication
Adequate human resources	Employee involvement

[From Henderson, 1989]

Most recently, Ashkenas, DeMonaco, & Francis (1998) identified the acquisition integration process framework that utilized by GE Capital Services, one subsidiaries of GE, which is the world’s largest in terms of market value. GE Capital grew through numerous acquisition transactions to become one of the world’s biggest financial services companies. Ashkenas et al, (1998) stated four lessons that they learned from GE Capital’s numerous takeover experiences. First, acquisition integration is not a distinct step of a transaction and should not begin only after the deal is done. Instead, acquisition integration and due diligence processes should be planned and should run together, and should be managed as an ongoing task. Second, Integration management is a substantial task and should be recognized as a discrete business function, equivalent to marketing, finance, or human resources. Third, immediate announcement and quick execution should be done regarding decisions about management structure, key roles and responsibilities, reporting relationships, layoff plans, restructuring plans, and other career-influencing post-acquisition plans. If these plans last for months, the expected benefits from a takeover will be substantially diminished. Finally, it is critical to realize that an acquisition integration plan deals with not only a wide variety of technical issues, but also the various cultural distances. A speedy and collaborative work is the best way to resolve business problems and achieve continuing, positive results. Ashkenas et al., (1998) also presented a "pathfinder model" that was developed by the GE Capital acquisition team over the years. Their model was comprised of four action stages in the overall process, with each action stage including several best practices. Each action stage possesses several subprocesses, which are detailed and practical activities that managers should follow to reinforce the process. The details of a "pathfinder model" are described in Table 22.

Table 22. A Summary of a PathFinder Model of GE Capital's Acquisition-Integration Process

Action Stage	**Subprocess**	**Best Practice**
Pre-Acquisition	1. Due Diligence 2. Negotiation & Announcement 3. Close	• Begin cultural assessment • Identify business/cultural barriers to integration success • Select integration manager • Assess strengths/weaknesses of business and function leaders • Develop communication strategy
Foundation Building	4. Launch 5. Acquisition Integration Workout 6. Strategy Formulation	• Formally introduce integration manager • Orient new executives to GE Capital business rhythms and nonnegotiables • Jointly formulate integration plan, including 100-day and communication plans • Visibly involve senior management • Provide sufficient resources and assign accountability
Rapid Integration	7. Implementation 8. Course Assessment & Adjustment	• Use process mapping, CAP, and Workout to accelerate integration • Use audit staff for process

		audits • Use feedback and learning to continually adapt integration plan • Initiate short-term management exchange
Assimilation	9. Long-term Plan Evaluation & Adjustment 10. Capitalizing on Success	• Continue developing common tools, practices, processes, and language • Continue longer-term management exchanges • Utilize corporate education center and Crotonville • Use audit staff for integration audit

[*From Ashkenas, DeMonaco, & Francis, 1998]*

A. APPROACH

Some types of mergers can be identified based upon a managerial perspective. Pritchett (1985) described the relationship between two merging firms as more or less co-operative, and offered four types of acquisitions: rescue, collaborative, contested, and raid. Schweiger & Ivancevich (1987) justified acquisitions as being mergers, planned divestitures, friendly acquisitions, or hostile takeovers. Walter (1987) identified four reasons for acquisitions: to pursue related diversification, increase competitive strength, maximize earnings, or limit risks. Napier (1989) proposed three types of mergers, including: (1) A characteristic of extension mergers is that the acquirer lets the target company behave independently with little or no change in its management team or operational standards; (2) Collaborative mergers occur when a combined firm generates benefits through a blend of operations, assets, cultures, and managerial functions (synergy-collaborative), or through a transformation of know-how, skills, and knowledge of each other (exchange-collaborative); and (3) Redesign mergers are characterized by the acquirer's intention for across the board alterations of major operational and managerial practices of the acquired firm.

The timing of human resource policy is important to the target firm. Searby (1969) suggested that changes should be immediate, upon consummation of the acquisition. Barrett (1973) recommended a phased approach, with the first three to six months used to retire or replace managers whose skills are no longer compatible with the combined firm's objectives, and the second 3-6 months used to adjust human resource policies. Managers of the acquiring firm must diagnosis resistance or fear of the target firms employees to the changing work environment, and must be well prepared by being equipped with appropriate strategies to overcome short and immediate problems after the deal closes.

Kotter & Schlesinger (1979) identified four key causes of the employees' resistance to change that occurs during initiatives, including parochial self-interest, misunderstanding and lack of trust, different assessments, and low tolerance for change. In order to overcome these problems, Kotter & Schlesinger recommended six solutions for facilitating smooth changes, including education and communication, participation and involvement, facilitation and support, negotiation and support, manipulation and co-optation, and explicit and implicit coercion. Often, acquisitions sink in the stormy seas of employee resistance based on resentment toward the acquirer, or even without significant structural or operating change, the deal can be vulnerable to an employee backlash simply because of the uncertainty created by a change in ownership or the existence of divergent aspects of the ways merging firms have been managed.

To make sure of pre-determined acquisition objectives, acquiring firms should establish an effective communication strategy to keep employees well informed and to provide them a comfortable working environment. Raab & Clark (1992) stated that, "Communications must be frequent and clear but should not unduly raise expectations," and "communications to employees need to start on the day the deal is announced and include the objectives and benefits of combination and the implementation process and time frames" (p. 20). Based upon good communication strategy, the acquirers should to integrate two different cultures and power systems, two different human resource policies, two different organizational issues, and two different operational strategies.

B. PEOPLE

The integration, retention, and motivation of key employees from merging firms is central to a successful acquisition. Some previous research has investigated the effects of acquisitions on a variety of management issues, such as culture (Buono, Bowditch & Lewis, 1985), structure (Mirvis, 1985), human resource policies (Profusek & Leavitt, 1984), and employee reactions (Wishard, 1985). Expertise in this area is critically important since acquisitions affect many stakeholders, including shareholders, customers, and employees (Marks, 1982; Rhoades, 1983). Shareholders are concerned because acquisitions ultimately affect their investments, particularly in the target firm (Lubatkin & Shrieves, 1986). Customers feel the impact of an acquisition when their neighborhood business becomes part of a larger organization, which may give the perception of being less personal. Employees typically receive the brunt of an acquisition’s impact, particularly if there is a massive layoff or are radical changes in the target firm (Napier, 1989). Bergsman (1997) provides a crucial suggestion for acquirers regarding the value of the target’s people by saying, “If IBM acquires Microsoft and Bill Gates decides to join another company, is IBM buying the full value of Microsoft?” (p. 60). Proper management of acquired personnel can have a tremendous impact on creating value for the acquirers.

There are some studies that have emphasized the importance of the human factor in acquisition success. For example, the results of many previous studies emphasized the phenomenon of the loss of autonomy of target managers, a situation which invokes tension and negative attitudes toward the acquisition (Levinson, 1970;Blake& Mouton, 1985; Perry, 1986), and which ultimately leads to post-acquisition integration problems and acquisition failures. Other studies highlighted the fact that conflicts and communication problems during acquisition may reduce the necessary devotion of the target managers and employees to the implementation of the post-acquisition integration process (Schweiger & DeNisi, 1991). Moreover, Leana & Feldman (1989) argued that the acquirers must become aware of managing the downsizing aspects of post-acquisition restructuring. The authors further stated that, “First, management should seriously consider alternatives to layoffs (e.g., changes in manpower or compensation practices) before proceeding with terminations. Failing that, corporations should make every effort to assist terminated employees through programs such as outplacement, severance benefits, and retaining opportunities. Also, the process of termination must be managed in a fair and equitable manner” (p. 138).

Marks & Mirvis (1984, 1985) identified the symptoms of “merger syndrome” as a key source of the disappointing results of otherwise well-designed acquisitions. “Merger syndrome” will hinder smooth post-acquisition integration and improvement of productivity, as well as increasing employee turnover. The authors classified merger syndrome into three dimensions, includes the personal, organizational, and cultural dimensions. Other dimensions include: (1) Personal preoccupation; (2) Worst-case scenarios; (3) Rumor-mongering; (4) Distractions from job performance; and (5) Psychosomatic reactions.

Awareness of human resources issues in acquisitions is important because human resource practices have influences on outcomes. Most human resources issues can be affected by acquisitions during the implementation stage. Because of this, implementation has been the primary area of human resource related research dealing with acquisitions. Primary topics investigated in the literature include the importance of formal, internal communications about an acquisition (Bastien, 1987; Graves, 1975; Perry, 1986; Schweiger & DeNisi, 1987), changes in organizational stucture (Adams & Shea, 1986; Mirvis, 1985), and problems of meshing different cultures and human resource policies (Gill & Fouder, 1978; Leighton & Tod, 1969; Marks & Mirvis, 1985). Ivancevich, Schweiger & Power (1987) identified some crucial implications of employees' personal stress by saying that:

> "Although merger-produced stress is inevitable, its effect can be minimized. Probably the biggest step that can be taken toward more effective management of merger stress is to become aware of how damaging are its consequences. Many employees do not have the resources and knowledge to effectively eliminate merger-produced stress; however, together organizations and employees can take specific steps to better control and minimize stress. The truth is that merger-produced stress has nor been on the "must do or must consider" agenda of management and human resource professionals. Statistics tell us that, although most mergers do not turn out as planned, management's success rate can be improved by doing something about employee stress" (p. 34).

Previous studies indicated personnel changes to be a critical acquisition success factor. Excellent management of post-acquisition personnel, including the target's top executives and various levels of employees, should be emphasized in a comprehensive inquiry in corporate acquisitions. The key to managing the post-acquisition integration process is "… to obtain the participation of the people" and "creating an atmosphere that can support (capacity transfer) is the real challenge" (Haspeslagh & Jemison, 1991, p. 106, 107). A key factor in creating such an atmosphere and obtaining people's participation during the integration process, involves the cultural differences between the merging organizations (Nahavandi & Malekzadeh, 1988; Weber & Schweiger, 1992; Calori, Lubatkin & Very, 1994).

Begley & Yount (1994) argued that the primary reason for the success of an acquisition can be the human side of the deal, especially in handling employee relations. Henderson (1989) argued that it must be recognized that the acquiring firms gain not only the target's land, buildings, equipment, and operations, but rather, people. Henderson further stated that:

> "General fear of the unknown and negative reactions to change and uncertainty can result in employee and management turnover that may reduce or impede the merger benefits. Altering potentially negative perceptions by emphasizing the opportunities for creative

> change and advancement accompanying a transaction will do much to reduce damaging employee reactions and enhance the prospects for post-acquisition success” (p. 32).

Hirsch (1987) found that managers felt personal instability during organizational restructuring, including acquisitions. Moreover, the negative impacts that acquisitions may have on employees and managers of the acquired company have been the subject of inquiry (Buono & Bowditch, 1989; Jick, 1979; Marks & Mirvis, 1985; Schweiger & Walsh, 1990; Schweiger & DeNisi, 1991). With regard to the treatment of the top management team of the target firm, there are different perspectives about the impact of replacement of executives of target firms and the impact of replacement on post-acquisition performance. Barney (1988) found that if a target firm’s executives’ expertise is valuable and unique, their retention is an essential determinant of post-acquisition performance. Moreover, Cannella & Hambrick (1993) found that since executives from acquired firms are critical resources, their retention is one of the crucial determinants of successful post-acquisition performance. This coincides with previous research findings (Pitts, 1976; Ravenscraft & Scherer, 1988; Lipton, 1985; Lowenstein, 1983). However, an opposite direction also has strong empirical results, showing that the replacement of incompetent executives is important in order to improve post-acquisition performance (Manne, 1965; Jensen & Meckling, 1976; Fama, 1980; Fama & Jensen, 1983; 1988; Walsh, 1989). Cannella & Hambrick provided a summary of previous studies in regard to this research problem, as shown in Table 23.

Table 23. Literature Summary of the Impact on CEO Retention in Acquisitions

Research Perspective	Arguments Identified	Implications for Performance
Manne, 1965; Jensen & Meckling, 1976; Fama, 1980; Fama & Jensen, 1983; Jensen, 1988; Walsh, 1988; 1989	Acquisitions represent a market for corporate control in which more competent executives displace less competent ones	Executive departure should have a positive effect on subsequent performance
Rumelt, 1974; Pitts, 1976; Salter & Weinhold, 1979; 1988	Acquisitions represent attempts to form unique and difficult to imitate combinations of resources. Relatedness implies synergy.	More relatedness implies that executives from acquired firms are more easily replaced by acquiring firms. In unrelated acquisitions, departure will be harmful to performance
Kitching, 1967; Jemison & Sitkin, 1986; Ravenscraft & Scherer, 1988; Yunker, 1983; Porter, 1987	Acquisition process is important to performance outcomes. Post-acquisition management is particular important	High departure rates may imply mismanagement of the post-acquisition processes, leading to disappointing performance outcomes
Barney, 1988; Walsh & Ellwood, 1991; Castanias & Helfat, 1991	Traditional views of relatedness are misplaced. Executives may have unique and firm-specific talents and skills	Executives from acquired firms are not easily replaceable, regardless or synergy. Departures are likely to be harmful to subsequent performance
Romanelli & Tushman, 1987	CEO turnover, considered in isolation, has no effect on subsequent performance	Departures, considered in isolation, will have no performance implications. Characteristics of the executives and the context must be considered
Grusky, 1969; Helmich & Brown, 1972	Outsider successors are more disruptive than are insiders	Departures are likely to disruptive, and may harm ongoing performance
Smith, Carlson & Alexander, 1984; Pfeffer & Davis-Blake, 1986	The abilities and skills of replacement executives have important performance implications	If able and experienced replacements are available, the negative effects of departure on subsequent performance may be lessened
Romanelli & Tushman, 1987; Virany, Tushman & Romanelli, 1992	The need for discontinuous change moderates the relationship between turnover and subsequent performance	The need for discontinuous change (in the context of poor preacquisition performance) may moderate the departure-performance relationship. Retention of more senior officers may be beneficial

[From Cannella & Hambrick, 1993]

Martin & McConnell (1991) found that the turnover of top executives increases significantly following acquisitions. Most importantly, the authors further mentioned that there is a strong correlation between management turnover and the pre-acquisition performance of targets. Martin & McConnell found that those targets with immediate management turnover significantly outperform those targets with unchanged management teams.

> "The importance of a well-planned thoroughly implemented post-acquisition strategy cannot be overemphasized. Acquirers often fail to realize fully the anticipated transaction benefits because they concentrate too much on the mechanics of making the deal happen and too little on what is required for success after completion. This is true regardless of transaction size"

The importance of an effective compensation program for merged firm's employees is frequently undervalued. Wood (1992) argued that compensation programs can facilitate productive relationships and focus on performance improvement, in both the pre- and post-acquisition phases, and can make a distinctive and valuable contribution to the ultimate success of corporate acquisitions. Wood suggested a set of compensation programs to match various types of mergers as shown Table 24.

Table 24. Four Acquisition Scenarios: General Recommendations for Compensation Programs

	Scenario 1: Target Firm (TF) Remains Autonomous	**Scenario 2: Target Firm is Partially Absorbed**	**Scenario 3: Target Firm is Completely Absorbed**	**Scenario 4: Merger Results in a Totally New Firm (NF)**
Salary Structure	• Maintain TF salary structure	• Maintain TF salary structure if TF and Acquiring firm (AF) business functions and markets are dissimilar • Use AF salary structure at TF if TF and AF business functions and markets are similar	• Use AF salary structure. Change titles and grades for TF employees as necessary	• Blend merger partners' salary structures to develop new, combined structure • Use new grade labels and titles to underscore new culture and break with the past
Pay Levels	• Maintain TF pay levels	• Adjust TF pay levels as necessary to align them with AF pay levels • If reductions are required, freeze TF pay levels until AF pay levels catch up	• Adjust TF pay levels as necessary to align them with AF pay levels • Accomplish reductions through pay-level decreases or freezes	• Reevaluate pay levels based on new business plan, culture, and selected peer group
Salary Administration	• Maintain TF salary administration	• Use AF salary administration to achieve consistency in administrative procedures and reports and to avoid having duplicate systems	• Use AF salary administration	• Develop new salary administration based on best features of merger partner's programs and practical needs of new entity
Performance Evaluation	• Maintain TF performance evaluation	• Use AF performance-evaluation system to achieve consistency in administrative procedures and reports and to avoid having duplicate systems	• Use AF performance evaluation	• Develop new performance-evaluation system based on best features of merger partner's systems and practical needs of new entity
Annual Incentives	• Continue separate TF annual incentives	• Design incentives so that some components relate to TF (operating-unit) performance and other components relate to AF performance	• Continue AF annual incentive programs and expand participation as appropriate to include TF employees	• Develop new plans that contain performance measures and goals that reflect NF's strategic financial plan and critical success factors

		• Weigh components to reflect the desired level of independence of TF (operating unit)		• Set incentive opportunity and participation levels to be competitive with marketplace at specified performance levels
Deferred Compensation	• Determine TF premerger deferred-compensation liability as of merger date • Modify TF programs if deferrals have been made in TF stock units. Consider interest equivalents equal to TF after-tax return on capital	• Determine TF premerger deferred-compensation liability as of merger date. • Use AF deferral program, if there is one, for TF postmerger deferrals • If there is no AF program, consider one or terminate TF program	• Determine TF premerger deferred-compensation liability as of merger date • Use AF deferral program, if there is one, for TF postmerger deferrals • If there is no AF program, consider or terminate TF program	• Determine premerger deferred-compensation liability for each merger partner as of merger date • Develop new deferral program that makes sense going forward
Long-Term Incentives	• Continue separate TF long-term cash plans • Convert any TF stock options or other stock-based incentives, or cash out if conversion is not possible • Develop cash plan or phantom-stock plan to replace TF premerger stock-based plan • Consider granting AF stock-based long-term incentives to TF to provide linkage between TF and AF	• Convert any TF long-term incentive program, or cash out if conversion is not possible • Develop new long-term contribution of TF (operating unit) with long-term contribution of AF, based on stated business goals and objectives • Grant AF stock-based long-term incentives to TF to provide linkage between TF and AF	• Convert any TF long-term incentive program, or cash out if conversion is not possible • Continue AF long-term incentive program and expand participation as appropriate to include TF employess	• Convert merger partners' premerger long-term incentive programs, or cash out if conversion is not possible • Develop new long-term stock-based incentive program to link compensation to the creation of shareholder value • Consider one-time all-employee grant to signal new culture and create performance orientation
Employee Benefits	• Maintain TF employee benefits or consider an eventual transition into AF benefits program to achieve cost savings and uniformity • Protect premerger TF vested benefits	• Adopt AF benefits program for TF employees to achieve cost savings and consistency across organization • Protect premerger TF vested benefits	• Maintain AF employee benefits • Protect premerger TF vested benefits	• Develop new employee-benefits program based on best features of merger partner's programs and practical needs of new entity • Protect premerger TF and AF vested benefits
Special Benefits/Perquisites	• Maintain TF special benefits/perquisites if they are reasonable	• Convert TF perquisites to AF perquisites over specified time frame, e.g., two years	• Convert TF perquisites to AF perquisites immediately or buy out	• Develop new perquisites package but minimize its importance to underscore performance orientation and reduce fixed costs

[From Wood, 1992]

There are certain common but negative reactions of employees in the target firm. There is widespread anxiety and stress (Ivanicevich, Schweiger & Power, 1979; Marks & Mirvis, 1985; Wishard, 1985), concern about job security (Mace & Montgomery, 1962), fear of decline in status or career prospects (Stewart, Wingate & Smith, 1963), and feelings of being 'sold out' (Black & Mouton, 1985). The target firm's top executives' attitude in the post-acquisition management stage has crucial impacts on success (Barney, 1988). Effective personnel management and the environment in which employees are considered as an integral part of the process are the core of successful post-acquisition integration (Henderson, 1989).

C. CULTURE

Culture has been defined by many scholars as the set of important assumptions, frequently unstated, that members of a community share in common (Sathe, 1985; Schein, 1985). Every group or corporation has an exclusive culture that is shaped by its members' shared history and experiences (Schein, 1985). In general, the uniqueness of the cultural aspect affects practically every area of the way people in a group interact with each other (Weber, 1996). According to Haspeslagh & Jemison, 1991), the key to managing the post-acquisition integration process is "… to obtain the participation of the people and creating challenge" (p. 106, 107). Cultural fit appeared to be a crucial factor in building such an atmosphere and gaining employees' commitment and involvement (Weber, 1996).

Culture is critical to the configuration of a total organizational structure, and influences the effectiveness of the organization in its internal environment. Therefore, in corporate acquisitions, culture can have an instrumental effect on both the coordination and control functions of integration, as it can operate to generate commitment to the larger organization (Siehl & Martin, 1981), can improve organizational soundness in a circumstance of radical change (Louis, 1980), and can carry out a sense of unity to the members of the entire organization (Deal & Kennedy, 1982). Among others, lack of cultural fit frequently is mentioned as a notable factor in acquisition failures (Nahavandi & Malekzadeh, 1988; Weber & Schweiger, 1992). Cartwright & Cooper (1993) stated that, "cultural fit and culture compatibility are well used but ill-defined expressions" (p. 60).

Weber (1996) argued that the existing literature on cultural fit has three primary limitations. First, most previous studies are based upon observations by practioners and consultants with little theoretical or systematic empirical evidence to support those observations (i.e., Barrett, 1973; Davis, 1968; Gill & Foulder, 1978; Leighton & Tod, 1969; Levinson, 1970; Pritchett, 1985; Rockwell, 1968; Searby, 1969; Sinetar, 1981). Second, relatively few empirical research has been conducted to investigate the cultural conflicts in only one acquisition (i.e., Blumberg & Wiener, 1971; Buono, Bowditch & Lewis, 1985; Graves, 1981; Dales & Mirvis, 1984; Shirley, 1973, 1977). Third, most prior studies were conducted under the assumption that acquisitions are homogeneous, and thus failed to consider the probability that the impact of cultural conflicts on their effectiveness might vary from one situation to another, even though acquisitions vary with respect to such variables as relatedness and type of industry (i.e., Lubatkin, 1983; Shrivastava, 1986; Nahavandi & Malehzedah, 1988; Weber, Lubatkin & Schweiger, 1994). Furthermore, Weber (1996) pointed out that previous studies do not provide systematic empirical evidence on the effects of cultural divergence on the effectiveness of the post-acquisition integration process, and on the post-acquisition financial performance of the acquirer.

Therefore, Weber (1996) pursued systematically the crucial but ignored role of cultural differences in corporate acquisitions based upon a relatively large sample, and Weber investigated the roles of other critical variables, such as the loss of autonomy, and the commitment of the target managers, to acquisition success. Weber adopted the top management team as the unit of analysis. Through his study, Weber (1996) provided the first systematic empirical evidence based upon a large sample size. The author identified firm evidence "on the relationships between culture clash, autonomy removal, and top management commitment to a merger and the effectiveness of the integration process and financial performance of the merged organization" (p. 1198). The study result was that, "the acquired manager's perceptions of cultural differences were found to be negatively associated with the effectiveness of the integration of merging banks, while autonomy removal and commitment were found to be positively associated with the acquiring firm's financial performance in the non-bank and full samples, respectively, and with effectiveness in the bank sample" (p. 1198).

Weber (1996) further explained that, "The strong effect of cultural differences in the bank sample is attributed to two factors. First, culture is important to service organizations because it serves as a potent control device in an otherwise highly uncertain and largely uncontrollable system. However, it is important to note that cultural differences were not associated with financial performance" (p. 1198). These finding are consistent with the results of the study of an acquisition transaction in professional service companies, where the human resource problems due to cultural conflicts did not cause long-term, post-acquisition financial performance (Greenwood, Hinings & Brown, 1994). Further, Pablo (1994) found that top executives in service companies were inclined to weigh cultural fit more heavily that top executives in manufacturing companies. Weber (1996) argued that, "Hence, it is possible that when top managers in the bank sample realized high cultural differences, because of the low effectiveness of the integration process, they took measures to deal with the culture clash and eventually financial performance was not affected" (p. 1199). Weber summarized the second reason as, "the effect of cultural differences in the bank sample may be related to the high level of autonomy removal, which is the consequence of a high degree of intervention in the decision-making of the acquired top management team in order to reap synergy potential. Thus, while a high level of autonomy removal may cause conflict due to autonomy loss and culture clash, a high level of intervention helps to cut costs and make the merged organization more efficient" (p. 1199). Weber (1996) concluded his study result as:

> "The conclusion from the results of this and other studies is that related mergers may be financially successful despite cultural differences, probably due to high synergy potential. However, it is clear from the results of this study that cultural differences have destructive effects, at least in the bank mergers, on the effectiveness of the integration process, and as shown in another study (Chatterjee, Lubatkin, Schweiger & Weber, 1992), on shareholder value. Thus, it is possible that mergers with similar cultures will outperform mergers characterized with disparate cultures. … The implication for practitioners is clear: the management of the buying firm should pay at least as much attention to cultural fit factors during both the premerger search process and postmerger integration process as they do to finance and strategic factors. This particularly important because the sample examined consisted of only related mergers that might have been supposed to yield higher financial benefit to the buying firms than unrelated mergers. At the same time, while higher levels of integration may be dysfunctional because they create conflict and reduce commitment of the acquired top managers to the success of the merger, it is possible that benefits due to synergy may be higher than the losses due to human factors. Therefore, the management of acquiring firms has to estimate both the synergistic potential of the merger and the cost of integration needed to realize the potential" (p. 1200).

Shrivastava (1986) identified three categories of the post-acquisition integration process: procedural, physical, and sociocultural integration. Procedural integration can be achieved by combining the operating systems of the two firms and then creating standardized and homogenized work procedures (i.e., legal and accounting integration, functional integration, and strategic business unit (SBU) integration. Physical integration is the process of integration of tangible assets, product/service lines, production systems, and core technologies. Shrivastava (1986) emphasized that the most problematic integration is cultural integration. Cultural integration takes place in management personnel and involves alignment of cultures and management philosophy (i.e., personnel transfer and organizational structure, sociocultural integration, gaining commitment and motivating employees, and establishing new strategic leadership). Shrivastava further stated that integration across departments involves: (1) coordinating activities; (2) monitoring and controlling activities; and (3) conflict resolving activities. Shrivastava (1986) created a framework of post-acquisition integration tasks, as shown in Table 25.

Table 25. A Framework of Post-Acquisition Integration Tasks

Post-Acquisition Integration Tasks	**Coordination**	**Control**	**Conflict Resolution**
Procedural	• Design accounting systems and procedures	• Design management controlling system	• Eliminate contradictory rules and procedures • Rationalize systems
Physical	• Encourage sharing of resources	• Measure and manage the productivity of resources	• Resource allocation • Asset redeployment
Managerial & Sociocultural	• Establish integrator roles • Change organization structure	• Design compensation and reward systems • Allocate authority and responsibility	• Stabilize power sharing

[From Shrivastava, 1986]

Cultural difference in corporate acquisitions is particularly important for the top executives whose motivation and commitment have a primary impact on the motivation among employees (Kitching, 1967; Perry, 1986; Sales & Mirvis, 1984). Schein (1985) argued that top executives play the most influential role in shaping and transforming corporate culture signals to the entire membership. Weber & Schweiger (1992) identified the consequences of management cultural clash in acquisitions as described by: (1) stress, distrust, and annoyance on the part of the target team in working with the acquirer team; (2) negative attitudes on the part of the target team toward the acquirer; and (3) negative attitudes toward cooperating with the top executives. Weber & Schweiger further stated that stress and negative reactions reduce the commitment of the target's managers to the smooth integration of the integrating firms, and their cooperation with the acquiring firm's top executives. Weber, Shenkar & Raveh (1996) found that, "The higher the corporate culture differentials, the lower the autonomy removal of the acquired company by the acquiring one. The probable explanation is that the perceived risk of joining highly different cultures is high" (p. 1223). This crucial cultural differences between merging firms causes negative financial performance by the acquiring firms after the deals (Chatterjee, Lubatkin, Schweiger & Weber, 1992), and may indicate the source of the high rate of acquisition failures (Cartwirght & Cooper, 1993). Most importantly, Weber, Shenkar & Raveh (1996) argued that this cultural difference is one of the most crucial causes of failures of horizontal acquisitions, compared to conglomerates and vertical acquisitions, which have seemingly less impact on cultural differences.

Marks & Mirvis (1984, 1985) identified the symptoms of "merger syndrome" as a key source of the disappointing results of otherwise well-designed acquisitions. Among the, cultural signs of the merger syndrome were: (1) Clash of cultures; (2) We versus they; (3) Superior versus inferior; (4) Attack-and-defend; (5) Win versus lose; and (6) Decisions by coercion, horse trading, and default.

D. ORGANIZATION

After closing the acquisition deal, a combining firm must realize that "the question as to whether this activity leads to an improvement in the allocation of resources and the efficiency of firms is still open to considerable doubt" (McKiernan & Merali, 1997). Organizational integration is complex. There are many factors that affect the effective integration between two firms, such as the firm's internal environment, core technology, size, management style and cultural norms and values, as well as impacts on uncertainties occurred from the external environment. Chandler (1962) stated that after diversifying their business areas, the studied firms realized the needs for altering their structure in order to achieve the intended maximum benefits, i.e., synergy. Chandler observed the effectiveness and efficiency of a new structure for firms: the divisional form. Through diversification and accumulation of their valuable resources, U.S. industrial firms have rationed their resources in order to meet short-term customer demands and long-term market trends. However, those firms had problems when they expanded their products or market regions through acquisitions, because they experienced difficulties in achieving their desired outcomes. One of the key reasons for this inefficiency in the acquirer's proprietary organizational structure, one that fit the old firm but was not effective for a combined company. A key change in terms of organizational structure was the role separation between headquarters and each business division. Headquarters executives focused their tasks toward the goal of combining long-term strategies of growth, while each division head was focused on his/her division's immediate and medium-term operational objectives. By adopting a new organizational structure, those organizations can achieve a continuity of superior utilization of their valuable resources.

In order to properly allocate resources for combined firms, an effective and efficient organizational structure is an essential to a successful acquisition. Clear organizational structures, reporting lines, and relationships in the work place must be established in the very first stage in the post-acquisition process (Henderson, 1989). To sustain potential competitive advantages earned from acquisitions, an appropriate organizational structure that allows effective resource allocation schemes must be a necessary process. Markides & Williamson (1996) stated that both short- and long-term competitive advantages are "conditional on an acquired company's putting organizational structures in place that allow it to share its existing strategic assets and transfer the competence to build new ones between divisions in an efficient manner" (p. 364). Markides & Williamson (1996) further argued that in order to achieve a successful related diversification strategy, "firms need to develop appropriate internal mechanisms for transferring competences and assets across business units in a more efficient way than can be achieved in the open market" (p. 364).

Markides & Williamson further stated that, "the story of contingency between diversification and structure is much more complex and subtle: researchers may not only need to measure relatedness in a different, more appropriate way, but may also need to unpack the concept of relatedness to examine its multiple dimensions and how they are separately related to organizational structure" (p. 364). Marks & Mirvis (1984, 1985) identified the symptoms of "merger syndrome" as a key source of the disappointing results of otherwise well-designed acquisitions. Among others, organizational signs of the merger syndrome were: (1) Crisis management; (2) Increased centralization (upward); (3) Decreased communication (downward); (4) War-room and combat mentality; (5) Interpersonal and intergroup tension; and (6) Less insight, more groupthink.

In order to establish a strategic synergy in a combined company, the acquirer may need to match its acquisition intent with its organizational structure. The acquirer's acquisitions intent must be embedded in the organizational design of a united firm. An ultimate goal of post-acquisition organizational design is to complement and support acquisition objectives through aligning all the components of a combined organization. The acquirer should consider the symmetry between the two aspects of a combined organization: the effectiveness and efficiency of the design in matching the organization's acquisition intent, and the combined structural influences on individuals, group relationships and the political dynamics of a united company (Nadler & Tushman, 1997). The differences between the acquiring firm and the target firm in the area of cultures, systems, and procedures continually hinder product design, marketing strategy, financial policies, and even day-to-day operations (Shrivastava, 1986).

For a combined company, its characteristic of organizational interdependency is one of the important aspects for a management team attempting to reduce the uncertainty and complexity caused by merging two companies. Thompson (1967) stated that a key element of a complex organization could be found in its organizational design. Through creating a rational structure, Thompson argued that an organization can overcome its bounded rationality. Thompson further identified relationships between different types of interdependencies and coordination efforts. Thompson identified three types of internal interdependence, including: pooled interdependence, sequential interdependence, and reciprocal interdependence. These three kinds, in the order introduced, have increasing degrees of contingency. The higher the degree of contingency, the higher the cost and the more difficult to coordinate. Thompson further introduced three coordination methods, which were: (1) standardization for pooled interdependence; (2) coordination by plan for sequential interdependence; and (3) coordination by mutual adjustment for a reciprocal interdependence. Thompson suggested that the core task of organizational structure is to minimize coordination costs and enhance coordination processes.

Combining Thompson's three types of internal interdependence and transaction cost economics, Jones & Hill (1988) attempted to understand three types of corporate diversification strategies and their counter-types of internal interdependence, as identified by Thompson, as mentioned earlier. The three types of diversification strategies adopted by Jones & Hill include related diversification, vertical integration, and unrelated diversification. Jones & Hill described three combinations of types of diversification and types of internal interdependence, including:

(1) related diversification and reciprocal interdependence; (2) vertical integration and sequential interdependence; and (3) unrelated diversification and pooled interdependence. Jones & Hill further stated that these three types, in the order introduced, involve increasing degrees of associated economic benefits. However, in terms of bureaucratic costs and transaction costs, the opposite is true. In sum, there are trade-off between economic benefits and bureaucratic costs among the three types of diversification strategies.

Integration of Information Systems. One of the most important areas to which acquirers should pay particular attention is information systems and network infrastructure, in terms of the compatibility and connectivity between the acquirer and target companies. Information systems (IS) can play a proactive role in the acquisition process by creating opportunities for achieving a competitive edge (Loverde, 1990), or by driving the organizational change process (Linder, 1989). McKiernan & Merali (1997) argued that IS infrastructure, "is a facilitator of operational and organizational integration (e.g., office communication, electronic mail, facsimile and telex; centralized order processing; automated warehousing; field marketing; etc.). In other words, without the IS/IT capabilities, integration of other operations could not realistically occur" (p. 62). However, less attention has been paid to the role of IS in firms engaged in acquisition activities (Weber & Piskin, 1996; Johnson, 1989; Bohl, 1989; McCatney & Kelly, 1984). McKiernan & Merali (1997) argued the importance of the strategic role of IS as:

> "The failure to pay attention to the strategic role of IS/IT in the merged entity precludes some organizations from exploiting IS/IT in its proactive capacity to reshape and reposition the organization in its competitive environment. Viewing IS/IT in a purely reactive role and allowing expediency of operational consolidation to drive systems integration have a detrimental effect, both on the quality of the organizational information infrastructure and on product quality. Redundant, incompatible systems may render the IS inflexible in the face of changing and emerging business needs" (p. 73).

In the study conducted by the American Management Association (AMA), two-third of the acquiring firms showed that their information was inappropriate in terms of making information-generated decisions concerning IS issues (Bohl, 1989). Furthermore, IS staffs are often not involved in pending structural changes until an official announcement is made (Bozman, 1989; McReil, 1989).

Many acquisition deals place an enormous burden on information systems (IS) staff to provide uninterrupted high quality services for a combined firm. IS managers of merging firms must know before the deal closes how the acquiring firm intends to integrate computer information systems with those of the target firm into a new, well functioning information processing infrastructure. Bruno (1995) proposed an action plan for IS managers who are facing acquisition deals by saying “to better prepare for a merger scenario is to standardize on limited sets of technologies while clearly defining staff roles and expectations” (p. 1). Stylianou, Jeffries, and Robbins (1996) stated that an information systems infrastructure must be evaluated prior to the acquisition, and the acquirer’s IS staffs must be involved during the entire evaluation process. The authors also argued that if there were no assurance of the involvement of IS professionals, potential problems raised in establishing integrated information systems will be inevitable and hence these problems will hinder the prospective efficient management of a combined company. The failure to conduct an ex-ante investigation of the target’s IS infrastructure is often cited as a key cause of why IS contributes to ex-post problems and/or obstacles (Carlyle, 1986; Fiderio, 1989; Johnson, 1989; Hoffman, 1990).

McKiernan & Merali (1997) found that, “fewer than half of the survey respondents had full information on software or voice and data communication systems” (p. 65). The reasons for this lack of preparation about IS are lack of time (Harvey, 1990), the low priority of IS functions compared to other functional activities (Harvey, 1990) or that the IS activities are not discussed or represented by the acquisition management team at the pre-acquisition phase (Loverde, 1990; Harvey, 1990). Moad & Carlyle (1988) identified that senior managers often view IS as the cost of doing business, rather than a significant contribution to their competitive effectiveness. McKiernan & Merali (1997) pointed out two crucial aspects of the lack of pre-formulation of IS integration strategies as:

> “Firstly, their absence can promote the development of fragmented systems which may result in a failure to develop consistent IS infrastructures which will remain effective in the face of changing business requirements. Secondly, their absence together with the absence of longer-term plans and a failure to make explicit the potential role of current IS staff in future development, may result in the loss of able staff” (p. 73).

Due diligence of IS infrastructure can be difficult and many firms are unaware of the total value of their investment in IS, including the value of software and data (Ryder, 1988). IS due diligence must be more than an inventory of the number of IS staff, hardware, software, and network capabilities of the target firm (Bohl, 1989). McKiernan & Merali (1997) pointed out that, “An evaluation of the IS development culture, the positioning of the IS function and the IS skills and training infrastructure of the target is often overlooked” (p. 67).

After the deal is closed, from the IS infrastructure viewpoint, the challenge is to establish a consolidated system that maintain a wide variety of primary functions that support other functional activities without interruption to employees and customers (Linder, 1989; Horton, 1989). There is a tendency for the acquirers to not fully consider the merits of the target's IS infrastructure (Violano, 1990). Previous studies have identified other IS related problems as cultural clash (Linder, 1989), and power distribution in the post-acquisition integration process (McKiernan & Merali, 1997).

In order to secure acquisition investments that capture synergies effectively, post-acquisition management must recognize the importance of IS (McKiernan & Merali, 1997). There is a close relationship between the overall level of integration and the level of IS integration. If the acquirer permits the target firm to operate independently, there may be a lesser degree of IS integration. However, if the acquirer wants to control the target comprehensively, the level of IS integration will be highly extensive. Giacomazzi, Panella, Pernici & Sansoni (1997) proposed a framework for IS integration strategies, as shown Table 26. The authors mentioned that, "The distinction between the different integration strategies is drawn by the standardization level of applications: i.e. the level of integration between IS depends especially on the number and kinds of business processes supported by the same software packages" (p. 291).

The failure to achieve IS infrastructure integration at an earlier stage can result in the setting of an unrealistic integration time-schedule and a lack of the necessary budget for operations consolidation (Fiderio, 1989). Other disruptions were, divergent IS technologies (Atkinson, 1990), data incompatibility and aged or inaccurately documented software (Carlyle, 1986), and the tendency for planners to render responsibility to operational staff with appropriate briefing (Linder, 1989). The heaviest cost during the IS integration stage is frequently associated with software conversion (Carlyle, 1986), whereas hardware and communication networks consolidation is relatively easy (McKiernan & Merali, 1997). Giacomazzi, Panella, Pernici & Sansoni (1997) identified that an IS integration strategy is not limited to only information management issues, but also includes organization, economics, and cost control factors. The authors further stated that:

> "Problems that can arise from the integration of two previously independent IS are mainly caused by choices regarding changes to the company structure after the transaction. First of all there are technical difficulties due to physical integration of the IS components and any lack of data compatibility. These problems can sometimes be solved by expensive investment and with

integration design involving the whole company. There are organizational problems, mostly depending on 'company structure'; these problems are difficult to solve and are often underestimated, while their solution would need good planning, a strong firmness by bidder management and sufficient time" (p. 290, 291).

It is important to be able to measure the success of IS integration. Stylianou, Jeffries, and Robbins (1996) stated that, "Successful IS integration was measured using the following variables: IS assessment of the success of the integration process and integrated systems, the ability to exploit opportunities arising from the merger, the ability to avoid problems stemming from the merger, and IS assessment of the end-user satisfaction with the integration process and the integrated system" (p. 209). The authors also identified four dimensions of post-acquisition IS integration success, as shown in Table 27.

Table 26. Influences on IS Integration Success

Influence	Description
Organizational Attributes	• Company size (i.e., assets, revenue prior to acquisition) • Number of employees (i.e., at time of acquisition) • Industry type (i.e., Primary end product/service) • Organizational structure (i.e., Functional, product, geographical, conglomerate, matrix) • Geographical distribution of decisions supported by the integrated systems (i.e., International, multi-state, single state) • Prior relationship between acquirer and target (i.e., Competitors, no business relationship, other)
IS Attributes	• Average number of IS employees at the time of acquisition • Quality of in-house technical skills in IS (i.e., State-of-the-art, advanced, average) • Geographic distribution of integration related IS activities (i.e., International, multi-state, single-state) • Distribution of hardware (i.e., Centralized, distributed, decentralized) • Level of data sharing across applications (i.e., Very high, high, moderate, low, very low) • Areas of major incompatibilities between merging firms (i.e., File/database architecture, applications, hardware, system software, programming languages, telecommunications)
Organizational Acquisition Management Issues	• Number of previous acquisition experience (i.e., More than one, one, none) • Degree of IS participation (i.e., Full, advisory, no participation, don't know) • Quality of Acquisition Planning (i.e., Excellent, good, average, poor)
IS Integration Management	• Desired degree of IS integration (i.e., Partial, full, no plans) • Current status of IS integration (i.e., Not started yet, partially completed, completed) • Target's IS operation audited prior to IS integration? (i.e., Yes, no, don't know) • Priorities established for integration systems? (i.e., Yes, no, don't know) • Importance of criteria by which IS integration priorities were established (i.e., Critically, very, moderately, slightly, not important) • Personnel-related changes resulting from the acquisition (i.e., Increases in IS workload, changes in IS policies and procedures, IS management turnover, decreases in IS workforce size, decline in employee morale, improvement in employee morale)

[From Stylianou, Jeffries, and Robbins, 1996]

Table 27. Matrix of IS Integration Strategies

Computer Architecture	**Totally Standardized Software**	**Partially Standardized Software**	**Adapted Software**
Totally Centralized	TI "A": Business processes are unified; all applications are standardized and the target company's computer system is located in the central data processing center of the bidder company; some computers can be sold or replaced. The data processing center of the target company is closed. The set of packages can be made up of all the bidder company's packages and applications or just a mix of those of both companies. Network connections must be dimensioned to support the data flow to and from the centralized data processing center. Databases may have to be converted to new standards on new packages at this time.	PI "A": This results in the total centralization of computers in one data processing center and partial standardization of business processes and of the software packages. Databases of the unified packages are translated to meet standards and new formats and are centralized. The other ones remain distributed.	Transition: This is a temporary solution that a company adopts for a certain time before deciding to adopt a deeper strategy.
Partially Distributed	TI "B": This represents similar characteristics; the main difference involves computers; the architecture of the new IS is not totally centralized but some computers that support special business processes, such as plants management and logistic, are left in their original location. In any case, the data processing center of the target company is closed and its staff reduced in order to cut fixed costs.	PI "B": This has the difference that computers here are partially decentralized, and software packages that have not been standardized run on these local computers; centralized applications run in the data processing center of the bidder company.	Transition: Same as above
Totally Distributed	TI "B": Same as above	PI "C": Involves a diffuse distributed IS architecture; the data processing center of the target company is not centralized and all software packages (standardized or not) run locally.	NI: The bidder company's strategy does not provide for any integration of the IS of the companies. All components are intentionally kept independent. The only linkages are those for transmission of data necessary for corporate management.

[Giacomazzi, Panella, Pernici & Sansoni, 1997]

To date, more and more companies utilize data warehouses as primary strategic information weapons. Corporate acquisitions make IS personnel and the end users, who rely on warehoused information, uncomfortable and/or worried (Stedman, 1997). For example, IS staff should take the time to dissolve different databases, data models and table entries such as accounting numbers and product codes. And end users may need special training to learn new terminology and methods of exploring information repositories (Stedman, 1997). Stedman (1997) identified some obstacles facing both IS staff and the end users in combining different warehouses, as shown in Table 28. As a real world example, the recent merger between HFS, Inc. and CUC International, Inc. revealed database consolidation problems due to the different data warehouses they have used. In order to maximize acquisition benefits through consolidating their databases, they should able to integrate their different databases, hardware and warehousing tools. It requires a lot of effort to interconnect HFS's data systems with CUC. One of the problems they are facing is that "whether it makes sense to build one aggregated data warehouse or have connecting data field among organizations that will remain largely independent" (p. 68, Hoffman, 1997). Stedman (1997) summarizes the some obstacles in integrating two different data warehouses. As shown in Table 28.

Table 28. Data Warehouse Merger Hurdles

For IS Department:	For End Users:
• Different databases, hardware and warehousing tools • Incompatible data models and database designs • Warehouses that focus on different types of information • Inconsistent terminology and table entry formats	• Functions may not be supported in new warehouse • Need to learn new data definitions and terms • Database design changes force new navigation methods • May need to switch query and reporting tools

[From Stedman, 1997]

Just as with the other operational or strategic issues in the post-acquisition integration phase, the lack of communication between merging firms can be lead to narrow objective setting (McKiernan & Merali, 1997). Harvey (1990) pointed out that decisions made for reasons of expediency of implementation may impact negatively on the quality and effectiveness of systems. With respect to the issues of cultural fit within the IS arena, Linder (1989) pointed out that political and power structure issues are key determinants of integration success. According to McKiernan & Merali (1997), organizational and management's 'IS maturity' is a key determinant of successful post-acquisition IS integration. The authors also emphasized that the speed of precise alignment between business and IS strategies is important to generate the intended acquisition outcomes.

E. STRATEGY

Clearly defined post-acquisition strategy and its detailed tactics are also critical to achieve the expected synergies from corporate acquisitions. One of the most important factors in the stage of post-acquisition management is to have “an ambitious vision, understood and shared by shareholders and management alike. Leaders have a vision and strategy for achieving that vision that almost always extends beyond the immediate deal” (p. 40, Smith & Hershman, 1997). Smith & Hershman (1997) further stated that, “Many organizations try to merge but fail to translate the vision that guided the merger into a purposeful action plan, to define the organization required to execute it, or to combine or redefine the underlying management processes and systems” (p. 41).

Sirower (1997) emphasized the alignment between the strategic vision of pending acquisition and explicit operating strategy by saying that, “The operating strategy cornerstone determines where any contestability gains can occur. Given that most major acquisitions involve little pre-acquisition planning, most acquisitions have no real operating strategy on the day the deal is completed. Instead there is a restatement of the vision with comments about how good the ‘fit’ is between the assets of the acquirer and the target. But actions speak louder than words, and without an operating strategy the vision is just words” (p. 31). Sirower (1997) further argued that, “The operating strategy must address how the new company will be more competitive along the entire value chain of the businesses. Acquisitions are often an attempt to divert attention away from a failing core business with the hope that the acquisition might provide a miracle for the acquirer. If answers are not forthcoming to the contestability questions, what becomes obvious is a vision with no strategy that will increase competitiveness or generate performance gains” (p. 32).

After closing an acquisition deal, the acquiring firm must be able to enhance its competitive methods or to add other competitive methods to compete effectively in order to achieve its intended synergistic benefits and sustain its competitive advantages. A competitive method can be defined as a source of a series of positive cash flows over its economic life, and it constitutes a portfolio of particular forms of products and/or services (Olsen, Tse & West, 1998).

In the lodging industry, the enhancement or synergistic effects on a wide variety of competitive methods of the merged company can lead to its immediate- and/or long-term competitive position. Further, a combined firm can improve its operating strategy through the reconfiguration of its strategic and operational competitive methods. Table 29 summarizes examples of the lodging industry's competitive methods, as identified by Olsen (1998).

Table 29. Examples of Competitive Methods of Multinational Hotel Firms (1985-1996)

Major Competitive Methods	**Definition**
Frequent guest programs	Programs designed to build customer loyalty by providing special privileges and free travel opportunities to frequent guests
Strategic alliances	Efforts made by firms to formally cooperate in such programs as advertising and marketing, sharing products and customers, and financing activities designed to maximize hotel occupancy
Computer reservation systems	First pioneered by Holiday Inns, these programs work similarly to airline reservation systems. Designed to fill rooms at rates that maximize the revenue yield per room these programs also make it easier for the customer and travel agent to secure desired accommodations at appropriate prices
Amenities	Added products and services available to the guest once they have registered. Often included are toiletries and in-room services
Branding	Attempts by hotel companies to create and deliver new products to the customer. Often thought of as levels of service such as budget, economy, luxury and business class hotels. Each product is associated with specific products and services to differentiate it from the competition. Brands are available in several of these segments as well
Technological innovation	This method includes a wide array of advancements designed to improve the products and services offered by hotels. They include all elements of communication systems, decision support systems for management, accounting services, safety and security programs, energy and conservation programs, automated check-in and check-out service, etc.
Niche marketing and advertising	These programs were designed to zero in on specific target markets emphasizing special products and services to those markets
Pricing tactics	This method is generally viewed as discounting and yield management (maximize the revenue per room based upon demand projections)
Cost containment	The attempt to operate as efficiently as possible by reducing all costs associated with running a hotel
Service quality management	The attempt by hotels to improve service quality by such techniques as Total Quality Management, continuous process improvement, etc.
International expansion	As current markets become saturated, hotel firms seek expansion into new overseas markets
Travel agent valuation	This method seeks to improve relations with the travel agent industry in order to seek greater volumes of business. This includes agent reward and incentives schemes
Franchising and the management fee	This method of growth is viewed as a competitive method for those firms that possess unique capacity to deliver the necessary capabilities in each case
Employees as important assets	This method places new value on the role of the employee in

	delivering and executing the delivery of high quality products and services
In room sales and entertainment	The method offers an array of possibilities to improve the revenue yield of each rented room by providing such items as pay-per-view on demand movies, beverages, snacks, and concierge services
Special services for frequent guests	This program goes beyond the early frequent guest programs and offers such attributes as automated check-in and check-out. Special seating, lounges, merchandise discounts in the hotel, and overall improved choices and upgrades for all products and services
Conservation/Ecology programs	Methods in this category are designed to address the guests' growing awareness of conservation and include examples such as clean air in the hotel and its rooms. It is seen as away of attracting guests who value these efforts
Business services	Designed to meet the needs of the increasingly pressured business travelers, these methods include a full range of business services in the hotel and room as well as a full range of communication services
Database management	This method takes advantage of growing technological capabilities to fully track the guest and his/her habits. This information is now being fully integrated into all other information systems utilized by the hotel
Core business management	The recognition of doing just one or a few things well underpins this method. Firms have divested themselves of peripheral business units in order to concentrate on the core business of hotel management
Direct to consumer marketing	The information highway and advancing technology now make it possible for firms to sell directly to the consumer using information provided by database marketing programs. This method will grow in popularity as more travelers seek to make their own travel plans through such channels as the Internet
New product development	This method includes creating entirely new products like all suite-hotels
Brand repositioning	This effort includes developing a clearer image of the products and services that will be available in each of the brands of a company. It includes efforts to clarify the difference between luxury and business class hotels
Technology	Investment in technology appears to be more intense as firms begin to realize the growing influence of the convergence of the computer and telecommunications in both running and marketing the business
Diversification	This method is a reflection of the desire of most firms to spread risk and enhance value added. Movements into the time-sharing industry, senior living centers, cruise ships and other complementary businesses are examples of this method
The value adding management change	Many companies responded to capital market pressures and hired new chief executives and top management who had successful track records in being able to add value to the firms they managed
Database marketing	The use of this marketing technique became popular in attempts by firms to capture the customer in a more individualized manner
Management information systems	Growing reliance on information for decision making

[From Olsen et al, 1998]

In sum, Henderson (1989) identified a set of key success factors for successful post-acquisition integration: (1) communication; (2) transformation plan; (3) transformation team; (4)

goals and objectives; (5) organizational structure; (6) specific targets; (7) priorities; (8) appropriate resources to achieve targets; (9) employee improvement; (10) employee layoff criteria; (11) win/win resolutions; (12) employee participation. Furthermore, Smith & Hershman (1997) suggested some important implications of post-acquisition management as:

> "A good first step in a plan for real growth is acquisition. For some firms, acquisition may be a way to achieve growth and a competitive edge more rapidly and less expensively than growing internally. Acquisitions, if they are managed properly after the deal is done, can be a solid basis of a grown plan that creates value. The weak spot in an acquisition is right after the deal is completed. That is when companies face value-killing indecision and aimlessness. Failure to move quickly to put the companies together will destroy the value the company hoped to gain in the first place. Successful buyers integrate swiftly and decisively to make the deal work. The earlier and more thoroughly that integration program is mapped out, the greater the odds are for ultimate success" (p. 39).

Post-Acquisition Performance Evaluation Criteria

After an acquisition transaction, the acquiring company must be effective in determining the anticipated synergistic benefits contributing to improving the overall performance of the firm. It is important to evaluate post-acquisition performance corresponding to the acquisition transaction for both the short-term and long-term value of the firm, based upon pre-determined and precise evaluation criteria. Almost unanimously, financial measures are the most popular method of evaluating to evaluate post-acquisition performance. Cochran & Wood (1984) stated that although there is no real consensus on the identity of the proper measure of financial performance, such measures fall into two broad dimensions: accounting profits and stock returns.

Accounting Profits. Accounting profitability (i.e., profit/sales ratio, return on equity, and return on net assets, which is a type of traditional measure of post-acquisition performance, are used as indicators of post-acquisition performance, but they are affected by biases and distortions. Meeks & Meeks (1981) argued that accounting profitability inherently possesses biases and distortions, including changes in the bargaining power of merging partners, changes in sales to one other's customers, changes in tax implications, gearing ratios or leverage ratios, changes in accounting norms in the year of the acquisition, and changes in goodwill arising from the acquisition. However, Grant, Jammine & Thomas (1988) argued that, "Our justification for using accounting returns was, first, that managers and external analysts often use return on assets as a measure of the effectiveness and efficiency of top management; second, the impact of corporate strategy on a firm's performance is more directly reflected in accounting profit than in stock price, which measures investors expectations about future profits. To test the robustness of our results, we also used other measures of accounting profitability, including total operating profits, return on equity, and return on sales. Those measures gave results similar to those for return on net assets, although their statistical significance was generally lower" (p. 781).

Stock Returns. Many previous studies that focused on acquisition performance utilized stock price changes surrounding acquisition announcement dates, based upon the market efficiency theory that stock prices fully appreciate to the likelihood of synergistic benefits from the acquisition (Dodd & Ruback, 1977; Kummer & Hoffmeister, 1978; Dodd, 1980; Asquith, 1983; Bradley, Desai & Kim, 1983; Jensen & Ruback, 1983; Malatesta, 1983). Cannella & Hambrick (1993) pointed out that the reason for the popular utilization of the above incomprehensive measure is that, "there is little public information available on the performance of acquired firms after the acquisitions has been consummated" (p. 144). Relatively few studies have investigated the long-run performance of acquiring firms after acquisitions, which means after the acquisition effective date (Franks, Harris & Titman, 1991; Agrawal, Jaffe & Mandelker, 1992).

Based upon numerous previous studies in measuring post-acquisition performance, the near-unanimous agreement was that target company shareholders' benefit the most from acquisition transactions, rather than the acquiring company shareholders. Ironically, based on this information, we can assume that the anticipated benefits are normally transferred from the acquiring firm's shareholders to the acquired firm's shareholders in takeovers because of the acquisition premium offered by the acquirer to the target. Moreover, the share price of corporate acquisitions indicates that acquiring companies generally break even, and that the combined companies' equity value improves as a result of acquisitions because of the synergistic benefits from takeovers (Healy, Palepu & Ruback, 1992).

However, there are some critical drawbacks to using stock price in measuring the post-acquisition performance of the acquiring firm. Caves (1989) argued that stock price perspective studies have had little success in relating the market value of equity gains to improvements in corresponding corporate performance. This implies that the equity value gains could be due to capital market inefficiency stemming from the production of an overvalued security (Healy et al., 1992). In order to determine whether success or failure in acquisition bids are from real economic gains or capital market inefficiencies, share price research has analyzed unsuccessful acquisitions (Dodd, 1980; Asquith, 1983; Dodd & Ruback, 1977; Bradly, Desai, and Kim, 1983, and Ruback, 1988).

Healy, et al., (1992) pointed out some of the flaws of the stock price perspective in measuring corporate post-acquisition performance. First, the authors argued that share price studies are unable to differentiate between pure economic gain and deviation from the market efficiency theory, called the market inefficiency paradigm. That is, from the share price standpoint, the expected real economic benefits are seemingly equal to the market's mispricing conception. Thus, it is hard to visualize a pure share price perspective that would explicitly explain the ambiguity of interpreting the indication. Second, Healy et al., pointed out that stock price studies lack explanations of the sources of acquisition-related benefits based upon the evidence. The authors argued that the sources of acquisition benefits can derive from such things as operating synergies, tax savings, or increased monopoly rents.

Operations Cash Flow. Healy, Palepu, & Ruback (1992) examined post-acquisition performance for the fifty biggest U.S. acquisition transactions, including Holiday Inns/Harrahs transaction in the hotel sector in the 1980s, between 1979 and mid-1984. The authors utilized the post-acquisition cash flow performance of acquiring and target companies. Healy et al., argued that "our research is motivated by the inability of stock performance studies to determine whether takeovers create real economic gains and to identify the sources of such gains" (p. 135, 136). More specifically, the authors used pretax operating cash flow returns on assets to measure improvements in operating performance. Healy et al., further stated that:

> "Conceptually, we focus on cash flows because they represent the actual economic benefits generated by the assets. Since the level of economic benefits is affected by the assets employed, we scale the cash flows by the assets employed to form a return measure that can be compared across time and across firms. We measure assets employed using market values, which represent the opportunity cost of the asset. In our opinion, market-based measures of asset values dominate accounting and other historical estimates in this context because they simplify intertemporal and cross-sectional comparisons. Our market-based measure has a potential limitation, however, because unexpected cash flow realization can change expectations about future cash flow, and hence market values" (p. 139).

Furthermore, Healy et al., (1992) defined operating cash flows as "sales, minus cost of goods sold and selling administrative expenses, plus depreciation and goodwill expenses" (p. 139). Healy et al., further stated that:

> “This measure is deflated by the market value of assets (market value of equity plus book value of net debt) to provide a return metric that is comparable across firms. Unlike accounting return on book assets, our return measure excludes the effect of depreciation, goodwill, interest expense and income, and taxes. It is therefore unaffected by the method of financing (cash, debt, or equity)” (p. 147).

Unlike Ravenscraft & Scherer (1987), who studied only acquired firms’ post-acquisition performance, Healy et al., (1992) integrated data about pretax operating cash flows for combined firms, for both the acquiring company and the target company, in each of the five years before the acquisition (-5 to -1). Similarly, post-acquisition operating cash flows were the actual values gained by the united firm in years 1 to 5. The authors further stated that, “We deflated the operating cash flows by the market value of assets. Operating cash flow returns are the ratio of operating cash flows during a given year to the market value of assets at the beginning of that year. The market value of assets is recomputed at the beginning of each year to control for changes in the size of the firm over time. For premerger years the market value of assets is the sum of the values for the target and acquiring firms. The market value of assets of the combined firm is used in the postmerger years. We exclude the change in equity values of the target and acquiring firms at the merger announcement from the asset base in the postmerger years” (p. 142). Details about operating cash flow returns are specifically classified into both operating and investment characteristics, as shown in Table 30. The authors also utilized industry-adjusted cash flow returns to measure whether or not the combined company’s post-acquisition operating cash flow returns outperformed its industry in the post-acquisition period. Most importantly, the authors integrated accounting and stock return information in a consistent pattern in order to produce high quality hypothesis testing methods in takeover inquiries, through investigating the correlation between the post-acquisition cash flow performance and the acquisition-related stock market performance. This productive and general approach was adopted by previous researchers to investigate corporate acquisition activities (Tehranian & Cornett, 1991; Linder & Crane, 1991).

Table 30. Definition of Variables Used to Analyze Actual Performance of Acquisitions

Variable	**Definition**
	(A) Operating characteristics
Cash Flow Margin On Sales	Earnings before depreciation, interest, and taxes as a percentage of sales
Asset Turnover	Sales divided by market value of assets at the beginning of the year (the market value of common equity plus the book value of debt and preferred stock)
Employees Growth Rate	Change in number of employees as a percentage of number of employees in the previous year
Pension Expense/Employees	Pension expense per employees
	(B) Investment Characteristics
Capital Expenditure Rate	Capital expenditures as a percentage of the market value of assets at the beginning of the year
Asset Sale Rate – Cash Value	Cash receipts from asset sales as a percentage of the market value of assets at the beginning of the year
Asset Sale Rate – Book Value	Book value of asset sales as a percentage of the market value of assets at the beginning of the year
R&D Rate	Research and development expenditures as a percentage of the market value of assets at the beginning of the year

[From Healy, Palepu, & Ruback, 1992]

Cornett & Tehraian (1992) investigated the post-acquisition performance of a large banking industry acquisition transaction between 1982 and 1987. The authors also examined the correlation between cash flow performance and the stock market performance of the firm. The authors acknowledged that this approach permits decisions about whether stock market gains accompanied with acquisition announcements are the result of pure economic profits, and thus implying that the sources of any acquisition-related benefits, even though the accounting information are not perfect measures of economic performance of acquisition transactions.

Cornett & Tehraian (1992) used operating cash flow (termed as earnings before depreciation, goodwill, interest on long-term debt, and taxes) divided by the market value of assets (termed as the market value of common stock plus the book value of long-term debt and preferred stock less cash), to measure performance. The author further developed seven banking industry-specific performance indicators in order to identify the origins of post-acquisition benefits in cash flow performance, as shown Table 31. Moreover, the authors developed detailed measures, which denote seven performance indicators, and defined terms, as shown in Table 32.

Table 31. Seven Common Bank Performance Indicators in the Banking Industry

Indicator	**Definition**
Profitability Indicators	Measure overall performance
Capital Adequacy Indicators	Measure the bank's ability to meet regulated capital standards and still attract loans and deposits
Credit Quality Indicators	Measure the changes in the bank's loan quality
Efficiency Indicators	Measure the bank's ability to generate revenue, pay expenses, and measure employee productivity
Liquidity Risk Indicators	Measure the change in the bank's cash position
Growth Indicators	Measure the bank's change in assets
Interest-Rate Risk Indicators	Measure the bank's exposure to interest rate risk

[From Cornett & Tehranian, 1992]

Table 32. Definitions of Ratios to Analyze Actual Performance in Bank Acquisitions

Ratio	**Definition**
Profitability Indicators	
1. Return on Assets	Net income after taxes as a percent of book value of total assets
2. Return on Equity	Net income after taxes as a percent of book value of total equity capital
Capital Adequacy Indicators	
3. Capital to Assets	Primary capital as a percent of book value of total assets
4. Loans to Equity	Total loans as a percent of book value of total equity capital
5. Deposits to Equity	Total deposits as a percent book value of total equity capital
Credit Quality Indicator	
6. Charge-Offs to Loans	Net charge-offs on loans as a percent of total loans and leases
Efficiency Indicators	
7. Expenses to Revenues	Operating expenses as a percent of operating revenue
8. Assets to Employees	Book value of total assets per full-time employee
9. Income to Employees	Net income after taxes per full-time employee
10. Return on Loans	Interest and fees on loans as a percent of total loans
Liquidity Risk Indicators	
11. Loans to Assets	Total loans as a percent of book value of total assets
12. Liquidity Ratio	Cash and government securities as a percent of book value of total assets
Growth Indicator	
13. Asset Growth Rate	Change in book value of total assets as percent of book value of total assets in the previous year
Interest-rate Risk Indicator	
14. Net Interest Income to Earning Assets	Net interest as a percent of book value of total earning assets

[From Cornett & Tehranian, 1992]

Operating Efficiency. Linn & Switzer (1994) found that acquirers experienced significantly worse industry- and size-adjusted operating performance for up to five years following an acquisition transaction. Brush (1996) found that operational synergy is a key reason for acquisitions and a determinant of post-acquisition performance. Since this study only focuses on horizontal acquisitions, post-acquisition operating efficiency is the key for achieving the anticipated synergistic benefits for a merging company. As previously mentioned, three types of synergies are identified. First, financial synergy is aimed at achieving a lower cost of capital through lowering the systematic risk to the acquirer. Second, the goal of operational synergy is to achieve operational excellence from the combined firm’s operations. Third, managerial synergy enhances a target’s competitive position by transferring management expertise from the bidder to the target. Operating efficiency can be achieved primarily through capturing operational and managerial synergies.

Market Share. Many previous studies used market share and changes in market share as measures of competitive performance (Buzzell, Gale & Sultan, 1975; Stigler, 1958). Brush (1996) argued that, “Market share and change in market share are the only measures of business performance available at the level of disaggregation necessary for intra-industry analysis at the business level of the firm for all manufacturing companies” (p. 8). Brush further stated that, “One advantage of using market share as a measure of competitive performance within each industry is that these conditions are held constant for the model and the findings can be interpreted with respect to the industry context. In other words, the findings can be further examined based on additional evidence of whether market share is a relevant measure of competitive performance in the industry” (p. 8).

Given the ambiguities and difficulties in assessing the precise impact of acquisitions on firm performance, it becomes necessary to identify appropriate key performance indicators of post-acquisition performance.

The Integration of the Overall Acquisition Process

As discussed in the preceding sections, acquisitions have been utilized as an instrument of value creation by many companies. Their rational choices about acquisition decisions, including strategic fit and organizational fit, probably were correct. However, based upon empirical studies, many previous acquirers have experienced failures to create value from their acquisition maneuvers.

The management’s acumen in the overall acquisition process has a vital role in maximizing value through acquisitions. As Jemison & Sitkin (1986[1]) indicated, the acquisition process itself has the most crucial role in creating value through acquisitions. Furthermore, deriving from Quinn (1981), the acquirers must be able to constantly integrate the simultaneous incremental processes of acquisition strategy formulation and implementation. In general, there are two primary stages in the overall acquisition process, including pre-acquisition management, and post-acquisition integration management, after the acquirer has initiated its acquisition intent.

According to previous research, there are numerous reasons for acquisition intent. The acquisition intent of the acquirer can be instigated by a variety of motives and/or objectives. The most frequently mentioned buzzword in acquisition activities is “synergy.” A primary argument for synergy is that by combining two business entities, the untied firm can enhance value through scale economies and cost savings. However, as Chatterjee (1992) argued, through restructuring the target by the acquirer, the merged firm can achieve increased shareholder value, rather than by the expected synergies between the acquirer and the target.

In the pre-acquisition management phase, as developed in this study, there are four crucial dimensions that co-exist and which substantiate the acquisition intent of the acquiring company. First, the acquirer must be able to gather reliable and valid information. In order to materialize the acquisition intent, acquiring companies should be able to gather, analyze, and synthesize a wide variety of facts and data necessary to reinforce a purchasing decision. Second, the acquirer must be able to identify the realistic value of an acquisition transaction. Value will be created from acquiring firms’ accurate calculation about the worth of a combination. Third, the acquirer should pay an appropriate price for the target firm. Overpayments, usually through acquisition premiums, will undermine the acquiring firm’s shareholder value, rather than enhance value. Fourth and finally, the acquiring firm must be able to develop a proper acquisition approach to materialize the acquisition’s objectives. The optimal development of a variety of surrounding procedures can facilitate an acquisition deal and, ultimately, can improve post-acquisition performance.

After the acquisition deal is completed, the combined management must be able to integrate well the formerly two different business entities. This study has developed five dimensions in the post-acquisition integration phase. First, the acquirer should be able to reconcile pre-determined acquisition objectives to the target, while avoiding unforeseen problems and obstacles. For example, the introduction of an extensive communication strategy can promote the comprehensive involvement and understanding of all employees during the transition process. Second, acquiring firms must be able to mitigate the personal stress of the target employees and motivate them to participate in materializing the acquisition intent. Third, the combined firm should also be able to mitigate their formerly different organizational cultures.

For example, quickly assimilating the acquiring firm's fundamental assumptions, such as norms and values, into the target firm is an effective integration strategy. Fourth, the merged firm should be able to integrate a wide variety of organizational configurations, including formal and informal structures, systems, and processes. Fifth and finally, the united firm must be able to create better operating strategies that represent a set of consistent alignment efforts to achieve the long-term goals of materializing the acquisition intent.

In addition, acquiring firms must develop an acquisition strategy based upon pre-determined, definite post-acquisition evaluation criteria. Financial measures should be utilized to identify whether or not value creation was realized. In general, as Cochran & Wood (1984) identified, there is no consensus on an appropriate measure of post-acquisition financial performance. This study will utilize five areas of financial performance for hotel acquirers, including accounting profits (i.e., ROE, ROA), stock returns, market share, operating efficiency (i.e., Occupancy, RevPAR), and operations cash flow.

Based upon the three phases and fifteen dimensions illustrated in Figure 1, this study will attempt to identify what specific factors (or operational indicators) have relatively important roles in the overall acquisition process to create value for shareholders. Among numerous factors, each possesses its own unique value and has its own impact on the hotel acquisition process, identification of the relative importance of these interrelated factors is the primary objective of this study. Thus, asking questions about what specific factors in the acquisition process have crucial impacts on successful acquisition is an appropriate inquiry for an exploratory study. As a pioneering study in the area of corporate acquisitions in the lodging industry, it is believed that a holistic approach along with a multi-dimensional framework is a more appropriate research method than narrowly oriented methods, i.e., one issue at a time and/or rational choice research perspectives.

As shown in Figure 6., when hotel firms initiate acquisition deals, they should realize the importance of the acquisition process and the integrated and incremental nature of the acquisition process to create value for their shareholders. In order to create value through acquisitions, the supporting building blocks of the acquisition process, such as pre-acquisition management, post-acquisition integration, and post-acquisition evaluation, make up the foundation of value creation. An integrated and incremental acquisition process framework, as seen in Figure 1., can enhance acquiring firms' overall acquisition process effectiveness, and ultimately can enhance the post-acquisition performance of the combined firm.

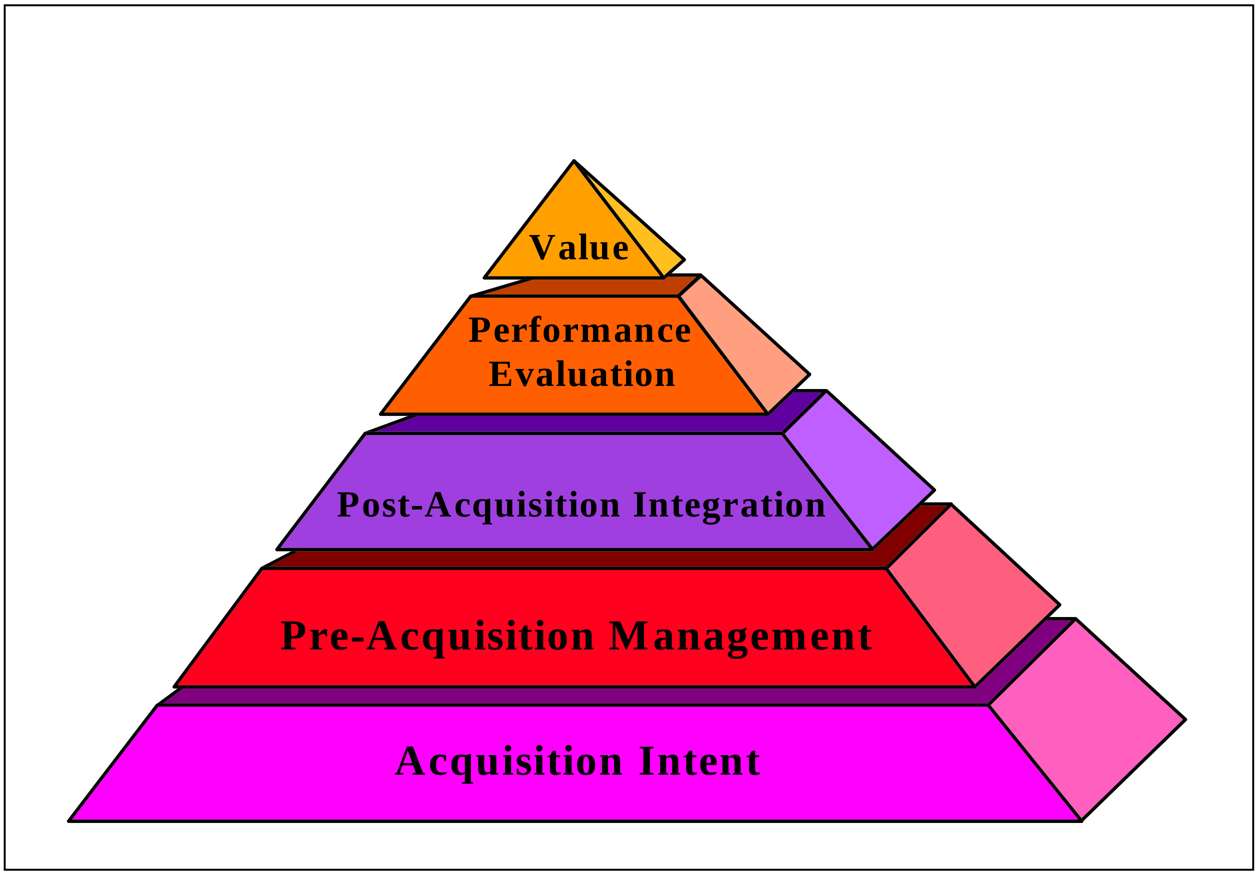


Figure 6. A Conceptualization of the Acquisition Process

Chapter Summary

To summarize, this chapter has comprehensively explored the factors affecting successful corporate acquisitions. Since there was no one study that examined the overall acquisition process in the lodging industry, this review primarily focused on the areas of strategic management, financial economics, financial management, and human resource management. In doing so, it was important to develop an integrated framework that could cover the above four academic arenas in order to generate sound empirical research results that would apply to the lodging industry, as well as to other industries' corporate acquisition studies. A brief discussion of the literature review follows:

First, the first two sections explored and introduced previous corporate acquisition research paradigms, including strategic management, financial economics, and human resource management. Through a historical review this study identified the evolution of corporate acquisition and its relationship with incorporated corporate strategies from the 1960s to 1990s.

Second, the next section explored previous corporate acquisition studies that attempt to discover post-acquisition performance of acquiring companies. The overall result was that many acquiring firms experienced disappointing results. In general, there is only a 50-50 chance for success in the corporate acquisition arena.

Third, this study broadly explored the causes and motives/objectives of corporate acquisitions. Many theories of corporate acquisitions were identified and a wide variety of acquisition motives and objectives were introduced and discussed. Because this study is limited horizontal acquisitions, the particular motives of horizontal integration were identified.

Fourth, this review identified previous studies' focus on influential factors and problems in the overall acquisition management process and its impact on post-acquisition performance. It was found that the process perspective is an alternative model that will replace the traditional and popular choice perspective. The process model is the one that emphasizes the role of the corporate acquisition process itself.

Fifth, key success factors and problems in both the pre- and post-acquisition management process and their impacts on post-acquisition performance were discussed. This section was divided into two parts, including both the pre-acquisition management process and the post-acquisition management process. In the pre-acquisition management process part, four constructs (or dimensions) were recognized, including information, value, price, and approach, and their corresponding factors or variables were identified and discussed. In the post-acquisition management process section, five constructs were identified, including approach, people, culture, organization, and strategy, and their corresponding variables were discussed.

Sixth, this chapter attempted to discover appropriate measurement criteria for post-acquisition performance. Since there is no real consensus on the proper measure of financial performance in the corporate acquisition research arena, it is important to identify various financial measurements to fit a particular industry, or all industries in general. This section identified five dimensions of post-acquisition performance evaluation criteria, including accounting profits, stock returns, market share, operating efficiency, and operations cash flow.

Seventh and finally, based upon discussions in the preceding chapter and upon previous research, this section reviewed the overall the acquisition process and the framework developed for this study.