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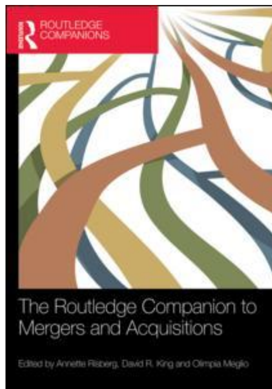

The Routledge Companion to Mergers and Acquisitions

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Conclusion

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Conclusion

Deconstructing M&A research – paradigm progress

Amy L. Pablo

Introduction

In 2002, a conference on mergers and acquisitions (M&As) (called the M&A Summit 2002) was held in Calgary, Alberta, Canada attracting scholars from around the world. At that time, we observed that there was a divergence between conventional academic wisdom and executive practice, and we recognized that existing research on M&As provided only a limited and insufficient understanding of this important phenomenon. While the construct is multidimensional and cross-disciplinary, most of the research was single-discipline and one-dimensional producing only a partial understanding of the phenomenon. A volume produced from that conference was published in 2004 (Pablo and Javidan 2004). That volume contained six parts, those being M&A Performance, M&A Strategy, Merger Implementation and Integration, M&A Knowledge Transfer and Learning, Culture and Leadership in M&As, and Research in M&As. The intent of the conference and resulting volume was throwing down a gauntlet to future M&A researchers by pointing out the need for better paradigm development, more attention to operationalization and measurement of key constructs, and importantly more multidisciplinary research utilizing methodologies that can capture the dynamics of the phenomenon under study.

The relevance of M&A clearly remains. In the 2000s, we saw what some have called a renaissance in merger and acquisition activity (Harding *et al.* 2013). In fact, at the beginning of that period we saw about 37,000 global M&A transactions with a value of about $3.5 trillion (Pablo and Javidan 2004). Those figures continued to grow until we saw a peak in 2007 when they surpassed 40,000 transactions valued at $4.6 trillion, but the global fiscal crisis brought that trend to a grinding halt. In the sobering light of the morning after, companies began to reconsider their use of this inorganic growth strategy more carefully, assessing the impact on their company's performance, and the whys of it. Given the high failure rates of M&As (estimated by some to be around 50 percent), one CEO opined: "In the end, M&A is a flawed process, invented by brokers, lawyers and super-sized, ego-based CEOs" (Baxter 2004, p. 1). Following the sea-change in activity levels after 2007, we began to see a more measured attraction to acquisitions.

Flash forward to today, and it is worth noting that in 2014 M&A activity is rivaling 2007 levels (Davis 2014), but the complexion of deals is a little bit different this time around. In fact,

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if you look at the deals being made, you'll see that the activity is not so geopolitically centric around the developed world (North America and Europe). By 2013, worldwide, M&As of more than 36,800 deals valued at $2.4 trillion were announced, with emerging-market companies taking a strong position in the deal-making race (accounting for one-quarter of M&A transactions); about 60 percent come from what are known as the BRIC countries (Brazil, Russia, India and China; Thomson Reuters 2013). The current companion volume takes the step of examining how the complexion of M&As is shifting. For example, the growing role of international acquisitions is considered in Chapters 7 and 11. The result is an increased recognition of the need to consider multiple perspectives in M&A research as the complexity of the phenomenon of interest continues to evolve. In sum, now is an appropriate time to assess where M&A research is at and where it needs to go.

What we have learned

In this present volume, approximately a decade after the M&A summit and associated volume, we address new areas to add a little more definition to the question of what exactly we are studying, how we are studying it, and to what purpose. In that quest, we delineate work relating to the Substantive domain of merger and acquisition research, the Contextual domain of merger and acquisition research, the Methodological domain of merger and acquisition research, and the Conceptual domain of merger and acquisition research. This addresses concerns expressed in the 2004 volume of M&A research that prior research was not cross-disciplinary or provided only a partial understanding of M&A (Pablo and Javidan 2004). In the 22 preceding chapters, we cover topics that focus on how M&As help firms to effect intentions relating to contextual needs presented by their changing environment, further develop M&A capabilities as needed and as required within their context, impact stakeholders such as employees and powerbrokers, and create new social networks and processes needing identification and further empirical research. Here, we set the stage for detailing what has occurred in the past ten years, and the broader picture of what we have learned, continue to learn, and need to learn more about. In the following paragraphs, I summarize a handful of topics that continue to be relevant.

M&A performance

Most observers of the M&A markets use shareholder return as the measure of deal success: it's easy to determine and it is easily understood. Thus, we have many researchers using event study methodology as a tool to measure the value-creating (or -destroying) effects of M&A. Some of the problems with this measure are that it is ex-ante, archaic, simplistic, uninterested, and uninformed. In other words, it is before anything happens to the combining organizations. It shows a blind faith in the financial markets, it doesn't take into account any of the difficulties an acquirer will encounter on this most difficult route, scholars don't want to invest the time and energy it takes to really understand the ex-post outcome, and they don't know how to isolate the impact of the deal. Thus, here we call for a more deliberate choice of measures and/or the use of multiple performance measures to enable rethinking what acquisition performance actually means, getting down to the level of investor behavior and decision making beyond the assumption of total rationality in the transaction. In fact, in Chapter 13 in the current book, we make a call for reorientation in the measurement of acquisition performance. Further, here we suggest the potential importance of managers' staying cognizant of changes outside the box of just their focal acquisition situation (i.e. put it in context: What's going on in the environment?).

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Finally, when we look at what senior executives actually use to determine acquisition success, these are factors that take time to become known. Only 5 percent say 6 months or less, and the majority say 1 year plus after the deal is completed. However, they do check how integration is going more quickly and regularly after the deal is done (*Intelligent Mergers* 2009). In other words, performance is not measured with either a single measure or at a single point in time.

Integration and synergies

In a review of M&As during the 2000s, models of M&A management that result in above normal total shareholder returns depended on the entire M&A process (Harding *et al.* 2013). Specifically, they found that repeatable models of successful acquirers include not only that they find, analyze, and execute the transaction, but, once the deal is done, they integrate the two companies. The importance of integration is receiving increased acceptance by executives. For example, in Bain & Company surveys between 2002 and 2012, integration challenges fell from the number one reason for disappointing M&A outcomes to number six (Harding *et al.* 2013). This reflects that successful acquirers devote more time, money, and attention to integration of the companies.

As explained by Pablo (1994), integration is the making of changes in the functional activity arrangements, organizational structures and systems, and cultures of the combining organizations to facilitate their consolidation into a functioning whole. The degree of change is dependent on what synergies are required to reinforce the corporate strategy behind making the merger/acquisition. Further, during the period of the 2000s researchers found that materiality mattered where the cumulative value of M&As amounted to a major percentage of the firm's market capitalization, such that the acquisition would command a more appropriate level of managerial attention and corporate resources. The impact of integration and associated issues reflected during integration are covered in Chapters 3, 15, 18, 20, and 21. Next, aspects of a paradigm for how to enact M&As for more profitable growth are outlined.

Strategic value

As shown in Chapters 1 and 5, M&As provide a way to acquire capabilities and pursue dynamic capabilities. Dynamic capabilities as described by Eisenhardt and Martin (2000) involve strategic organizational routines that enable firms to achieve new resource configurations or facilitate positive growth and development. To the extent that corporate growth is a valid strategic goal, M&As are a valid way to achieve them inorganically, potentially changing the organization in a beneficial direction along the way. In Chapter 5 of this volume, the authors describe M&As as a dynamic capability and describe how they involve a multi-layered temporally dependent process requiring multiple organizational mechanisms to ultimately result in a successful acquisition outcome. In that qualitative study, multinational companies were studied as a new venue for understanding the breakdown of how the acquisition capability is built from the ground up through organizational parts combining in processes and culminating in an acquisition capability which is dynamic enough to be used to reconfigure the organization on an as-needed basis.

In Chapter 9, M&As are looked at within their role in the whole corporate development portfolio where decisions are made about how to meet the organizational objective of growth. Developed routines lead organizations to choose between either exploiting a known growth strategy or exploring new avenues to gain resources (i.e. provide fuel for the engine of growth). The author examines the performance advantages that can be

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gained through appropriate selection and balancing of modes of growth, specifically building (organic growth/internal development), buying (mergers and acquisitions), or partnering (alliances and leasing), but also recognizes the different managerial challenges of each. The author suggests that more research is needed to better understand the impact of the chosen corporate development portfolio not only on firm survival, and also, taking a contingency view, under what circumstances what kinds of effects it will have, and what learnings can be gained by each.

Importance of learning

An example of a dynamic capability is an organization's ability to learn new practices or routines. Learning is a dynamic process that combines experimentation and repetition in a non-linear process aimed at improving both organizational efficiency and effectiveness (Eisenhardt and Martin 2000). An example of a dynamic capability is an organization's ability to learn new practices or routines. Learning is a dynamic process that combines experimentation and repetition in a non-linear process aimed at improving both organizational efficiency and effectiveness (Eisenhardt and Martin 2000). In the case of an acquisition capability, there must be continued codification of the knowledge held and assignment of managerial responsibility for intraorganizational transfer to key functional members of an acquisition team. As acquisitions are complex, with many dimensions influencing their outcomes, a number of studies have shown that at best 50 percent of acquisitions are successful. Thus it is that we see amongst the most successful M&As firms that have codified their acquisition activities. This is reinforced in the next section where some of the more and less successful M&As since the turn of the century are reviewed.

Continued lessons

Dramatic examples of success and failure continue to persist in M&As, and reviewing successful acquirers and specific deals that exemplify success and failure demonstrates that practice can continue to improve, while also highlighting areas for research.

Best M&As

Berkshire Hathaway (BRK) has made a reputation for being a successful serial acquirer. Probably because the acquisition process is so complicated and difficult, "serial acquirers" appear to be more successful with M&As than occasional acquirers (Douma and Schreuder 2013). Under the leadership of Warren Buffett, operating as a holding company, BRK acquisitions have been made solely for the purpose of gaining a controlling interest in another company, not for managing its ongoing operations, achieving synergy, or blending. Thus, integration is not a central issue for the success of these acquisitions. Financed largely by BRK's ongoing insurance firm holdings, Warren Buffett (CEO) has been able to spread the risk of his M&A investments widely. Considered to be the most successful investor of the twentieth century, he in fact is noted for his value-investing philosophy and his own personal frugality. In a famous quote from Buffett, he said: "Price is what you pay. Value is what you get" (Berger 2014). This is an apt description of the difference between market price (i.e. the price that the market requires to effect a transaction) and intrinsic value (i.e. the intrinsic worth of a business, which is a function of cash flow to be generated by the acquired business, which in turn is a function of core operations, expected synergies, integration success, and other factors).

In fact, BRK has set forth a stringent set of criteria for making business acquisitions, as follows:

1 large purchases (at least $75 million of pre-tax earnings unless the business will fit into one of their existing units);
2 demonstrated consistent earning power (future expectations are of no interest to them, nor are "turn-around" situations);
3 businesses earning good returns on equity while employing little or no debt;
4 management in place (they can't supply it);
5 simple businesses (if there's lots of technology, they won't understand it);
6 an offering price (they don't want to waste their or the seller's time bargaining).

This acquisition capability was used to great success in the 2000s, enabling BRK to complete what is considered to be their fabulous five. They represent Berkshire's largest non-insurance businesses and they are in a wide variety of industries including wind energy for electricity generation (MidAmerican Energy), coal transportation for electricity production (BNSF Railway), an Israeli metal-working company (Iscar), a tank car maker (Marmon Group), and a controlling interest in a chemical maker for $9 billion in cash in 2011 (Lubrizol). Buffett expanded that coverage into yet another industry, spreading his risk even further through his 2013 acquisition of Heinz for $28 billion in partnership with 3G capital. The lessons from BRK appear to be recognized by other businesses. For example, Cisco is another successful serial acquirer that has established criteria for acquisitions (Bunnell 2000), and acquisitions by firms in emerging markets involve less integration (Kale *et al.* 2009).

Another successful acquisition from 2008 that bears a more industry-specific strategic tone is the acquisition of Anheuser Busch by InBev. In fact, InBev resulted from a merger between the Belgian company Interbrew and the Brazilian brewer AmBev in 2004. The brewing industry world-wide has recently experienced consolidation, reflecting increased M&A activity, transforming the global beer industry. The Anheuser Busch InBev combination created the global leader in beer and one of the world's top five consumer products companies. In this case, a thorough integration of these two firms (taking nearly 3 years) was essential to realize necessary cost savings and synergies. Integration allowed them to realize over $250 million in cost savings and expected synergies of $2.25 billion even in the face of the global recession. The result was the world's largest brewer with 22 percent of global market share and 50 percent of US market share. This transaction also prompted the creation of even more consolidation in the brewing industry (e.g. Miller Coors and Molson Coors) through joint-ventures. This highlights the importance of competitor responses to acquisitions that is introduced in Chapter 19, but has largely not been considered by research.

Worst M&As

The $360 million AOL-Time Warner merger in 2000 was hailed at the time as a dream marriage of the old and new media. However, it quickly fizzled and became widely regarded as the deal that came to define the dot.com era. This was, at the time of the merger, considered to be evidence that the old and new media were converging, with internet companies doing the buying and the old media (including properties like Time, People, Fortune, Warner entertainment, HBO and CNN) doing the selling. Moving from old to new media can be seen as a journey in technology, and acquisition as a method of adaptation. In the buy-versus-build question, Time Warner thought that it had found a ready-made solution to its lack of internal digital capabilities in its suitor AOL, which had resources to burn. What went so wrong?

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First, there's the question of the cultures of the two organizations, being vastly different (the conventional and long-established representative of the print media world versus the innovative and liberating dot-com of the internet world). Normally, as a company matures from a startup to a more established company, the company culture changes. Additionally, as the environment in which the company operates (the laws, regulations, business climate, etc.) changes, the company culture also evolves. These changes may be positive, or they may not. The changes in company culture may be intended, but often they are unintended. They may be major changes or minor ones. The company culture will change, and it is important to be aware of the changes. Cultural conflict between AOL Time Warner reflected that the cultures were the products of companies at different levels of maturity and apparently different prospects for the future (Quinn 2009; Ray 2012). AOL and Time Warner essentially were two different societies at war with one another. Readers interested in related ideas can read Chapters 11, 14 and 21.

Second, even though they may try to, and pretend to work together, another issue at the heart of firms that can cause problems is managerial hubris. The AOL and Time Warner CEOs had to realize that there were differences, but they thought they could overcome not only the differences between their firms but also the inherent philosophical and age differences between the two. The result was an internal firm environment of essentially survival of the fittest, while the external environment around them was going through a foundational upheaval. Life as these people knew it was essentially being transformed. This wasn't just a merger of two businesses, or just related versus unrelated businesses trying to become one—this was a merger of necessity. Both of these companies were in the media business, but one of the parties to the merger (AOL) was being tremendously overvalued by investors who believed in its potential, while the other (Time Warner) had a proud past with dim prospects on its own. Again, this suggests that the competitive context of an acquisition is important; some of these issues are discussed in Chapters 12, 17 and 18.

Third, societal change compounded the problems of cultural issues and managerial hubris to contribute to the failure of AOL and Time Warner. As noted by McGeorge Bundy, an advisor to President Kennedy, "There is no safety in unlimited technological hubris" (Bundy 1987). Much like Alexander the Great, the CEOs of AOL and Time Warner considered themselves to be the gods of the media world, one which was denoted by promise, hope, efficiency, and speed, and the other by a consistent stable of performers. In the campaign for success in the battles of the old and new media, these CEOs wanted to claim their place in history. As with Alexander the Great, the reason for their exploits were not political but personal. Their quests, though of great genius, were made out of pure hubris. Like Alexander, they acted as if they were the sons of a god, because since early on the stock market had told them so. Their quests were for recognition by others but most of all by themselves. They each believed that they had made their places in history. According to Case from AOL, "This is a historic moment in which new media has truly come of age"; and, according to Levin of Time Warner, the Internet had begun to create "unprecedented and instantaneous access to every form of media and unleash immense possibilities for economic growth, human understanding and creative expression" (Arango, 2010). Little did they know it, but the dot-com bubble was about to burst, causing investors to abandon a problematic corporate combination like rats leaving a sinking ship. Again, the competitive environment of acquisitions is discussed in Chapter 19.

In the end, old and new media were not just of different cultures, they were different species that were inherently at war. Although they were both media companies, it was more a matter of how they operated or firm values. Firm values influence how a deal is done. In the case of AOL Time Warner, differences in values led to integration never taking place. Further, cultural conflict resulted from business units working against each other, reflecting a lack of trust between

the two that was constant and manifested harmful organizational practices. Unfortunately, similar cases of cultural clashes and hubris persist in acquisitions that destroy value, as demonstrated by the DaimlerChrysler merger (Krug *et al*. 2014).

Paradigm progress

With this new companion, the gauntlet thrown down approximately a decade ago has been taken up to substantively contribute to the development of M&A paradigms. Paradigm development is a theory or a group of ideas about how something should be done, made, or thought about. Beyond simply shifting between paradigms, progress likely depends on an interplay of paradigms that recognizes and contrasts perspectives to improve understanding (Schultz and Hatch 1996). Herein, we have included works that give more attention to operationalization and measurement of key constructs (i.e. Chapter 13) and, importantly, more multidisciplinary research utilizing multiple methodologies that can capture the dynamics of the phenomenon under study. For example, Chapter 14 outlines the application of institutional ethnography as a method for studying M&A.

Going forward, greater interplay of paradigms could facilitate reconciliation of the larger M&A phenomenon with different subgroups focused on technology, emerging markets, family firms, and so on. Further, comparison of perspectives focused within firms (i.e. capabilities) and external perspectives (i.e. competitive dynamics) could provide useful insights. M&As defy simple stereotyping, with the implication that research needs to evolve to consider emerging practices and offer insights to improve managerial practice. This means that there is a greater requirement for researchers to identify and examine current M&A practices. While there is absolutely a need for additional study, we believe that we have contributed substantially to M&A research and practice.

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