Impact of Culture on Mergers and Acquisitions: A Literature Survey

Dr. Bisma Afzal Shah
Research Scholar, Kashmir University, School of Business Studies, J&K, India

Abstract

Mergers and acquisitions are becoming a favoured path for organizations attempting to have competitive advantage over its competitors. Organizations all over the world spend billions of dollars in pursuit of this strategy. However, the success rate is less than what is expected. One of the reasons attributed to the same is the clash of corporate cultures. The cultural aspect of mergers and acquisitions has been identified as one of the key issues that may help explain the failure of many mergers and acquisitions. Yet what needs to be done to improve cultural integrationin order to enhance merger and acquisition success has received relatively little attention. This present study attempts to review the research studies and literature to examine the role played by culture and suggest a framework for better management of cultural differences.

Keywords:

Mergers and acquisitions, culture, integration

Introduction

Over the last two decades, mergers and acquisitions have become a global phenomenon and a popular strategic choice for companies' growth and expansion.Mergers and acquisitions (M&A's) have become an increasing means of strengthening and maintaining firms' position in the market. For it is regarded as the fast and efficient process of expanding into new markets, gain a competitive edge, or acquire new technologies and skill sets. Despite the increasing popularity of mergers and acquisitions, it has been reported that more than two-thirds of such deals fail. Researchers have proposed many explanations for such high failure rate of merger and acquisitions, yet one explanation which is often underestimated and is of special interest is the cultural element in M&A integration processes. After reviewing pertinent literature, it is clear that culture clashes between merging/acquiring organisations have been one ofthe most common explanations for the failure of mergers and acquisitions. It is true that mergers and acquisitions do fail due to the reasons of financial and economic nature; but making a merger or acquisition successful is more than 'getting the sums right'. Research studies have found that as many as 75 % of merger and acquisition deals fail to produce desired financial results because people do an inadequate job of engaging employees and integrating the culture of merging/acquiring organizations (Sperduto, 2007).Underestimating the importance of the cultural element is one of the key issues that may help explain the failure rate of many mergers and acquisitions.

Objectives:

- To study the impact of culture on mergers and acquisitions as exploredby several researchers in different countries.
- To suggest a comprehensive framework for better management of cultural differences in a merger or acquisition process.

Methodology:

The present paper is a review paper. Several papers on Cultural impact on mergers and acquisitions across various countries have been taken for the review.

Organisational culture

The word “culture” has many meanings and different definitions and there is no agreement among researchers as to its exact meaning. However, most academics either define 'national' or 'organizational culture'. One of the most influential and most cited scholars in the field of culture, Geert Hofstede (2001), defined “national culture” as a collective programming of the human mind that distinguishes the members of one group or category of people from another. On the other hand, 'organizational culture' is defined as a developing system of beliefs,values and assumptions shared by the members of an organisation about the desired way of managing the organization, so that it can adjust to its environment, Chatterjee et al. (1992), Lubatkinet al. (1999), Migliore(2011), Schein (1985), Weber (1996). Business etiquettes, organization structures, management styles, for example, belong to 'organizational culture'.

Organizational culture focuses on how organizational participants experience and make sense of organizations. It is defined as basic assumptions and beliefs that operate unconsciously and are shared by members of an organization. The concept of "shared" meaning is central in understanding culture. Organizational culture is learned by group members who pass it on to new group members through a variety of socialization and communication processes. The degree of cultural fit between two companies is a measure of the "shock" that employees will experience by entering a new organizational environment. This is called as clash of cultures (Mirvis& Marks, 1992). Something that it is easy to forget, is that organizations are composed of people. Changing external aspects such as name, brand, colors, technology, etc. also involve changing a symbolic world that used to be part of many people' own identity. This is one of the main reasons why M&A are difficult processes. They involve changes at all levels, starting by the individual level that affect the system of believes that the person is used to address.

One of the important aspect of cultural clash is acculturation. Acculturation is a process in which members of one cultural group adopt thebehavioursand beliefs of another group. Although, acculturation usually involves a minority group adopting the habits and language patterns of the dominant group, it can be reciprocal as well i.e., the dominant group can also adopt patterns typical of the minority group. Integration of one cultural group into another may be evidenced by changes in language preference, adoption of common attitudes and values, membership in common social groups, and loss of separate political or ethnic identification (Hazuda et al. 1998). According to Nahavandi and Malekzadeh (1993), the entire process of getting to know and function with another culture can be a highly positive experience, but many times it is accompanied by disruption and alienation for members of the less dominant culture and, in some cases destruction of entire cultures; with a feeling of unending conflict.

Literature Review

Steven H. Appelbaum and Joy Gandell (2003), analysed the impact of culture upon a health care merger. A case study of the merger of four well established hospitals into MLMC (Maple Leaf Medical Centre) was examined.It has been found that conflicts within the top management and an unclear communication resulted in decreased overall adjustment of employees and increased rates of failure. Human resource department did not follow the cultural plans of action.

Yaakov Weber and ShlomoYedidiaTarba (2012), on the basis of literature review and case studies of both successful and unsuccessful companies provided insights as to how the corporate culture had an impact during pre-merger stage, negotiation, and the post-merger integration process.It was concluded that the high rate of M&A failures was due to the lack of synchronized activities at different merger/acquisition stages. Further, the study provided different managerial tools that would help in better corporate culture assessment during all stages of M&A's, including screening, planning, and negotiation, and enhance the effectiveness of interventions carried out during post-merger integration process.For example, the assessment of culture differences during the stage of planning and evaluation of the profitability of a merger or acquisition, would help in determining the integration approach to be followed after the agreement, the time frame and the costs needed for integration, which in turn would serve to assess the ability to realize the synergy potential. Information about the extent of cultural differences and integration difficulties could facilitate the evaluations of expected cash flow, the anticipated effects on EPS, the effects on the change of stock prices after the agreement and the risk inherent in each alternative. During the negotiation process, managers identify expected obstacles in communication caused by differences in corporate culture and to acquire tools for the bargaining stages.During the integration stage, correct analysis of cultural differences would help to determine the choice of units that are to be integrated during the early or late stages of the process, according to the types and strength of the differences. In this way, during the different stages of M&A's, it is possible to compare the advantages and disadvantages of each candidate for merger/acquisition and when these cultural differences between the organizations become clear, it would be possible to define a desired shared culture for achieving better success.

Daniel Rottig (2007), examined the cause of failure rates in international M&A's in response to the cultural differences. The study has found that high failure rates of cross border M&A's were not due to cultural differences but because, firms most of the times were not able to combine dissimilar cultures due to poor management. Thus, the question is not whether to acquire companies in culturally distant market but how to do it successfully. The results have shown that there were four major determinants of successful cultural combinations: cultural due-diligence, cross cultural communication, connection and control. Time and again, cross-cultural management is mishandled by top executives in M&A's and eventually results in failure, as in the case of the Daimler Chrysler merger (Kuhlmann and Dowling, 2005).

Chaoyun Liu (2012), analysed the impact of national culture on post-merger performance.The results have been analysed using Hofstede's cultural measures (power distance, individualism, masculinity and uncertainty avoidance). It has been found that difference in individualism was positively related to merger performance whereas differences in other cultural aspects were negatively related.

Rajesh Chakrabarti, Swasti Gupta-Mukherjee and Narayanan Jayaraman (2009), studied the impact of culture on long term post-acquisition performance of the firms. They studied the impact of cultural differences using three measures: legal origin, religion and language. The study has shown that M&A deals involving culturally distant firms performed better in the long run. Culturally distant firms can spur innovation by helping break rigidities, prompt the firms to go for better screening, evaluation leading to more complete contracts between firms. Such cultural variations can thus be turned into huge business advantages.

Gunter K. Stahl and Andreas Voigt (2008), provided a review of theoretical perspectives and empirical research on the role of culture in mergers and acquisitions. The review has revealed mixed results.Empirical evidence indicated that the differences in national and organizational cultures were often associated with negative outcomes at the socio-cultural level, such as increased top management turnover, reduced employee commitment etc. However, the impact of cultural differences on financial performance was found to be less clear. While some studies found cultural differences to be negatively associated with accounting or stock market based performance measures, others observed a positive relationship or found cultural differences to be unrelated to post-acquisition performance, indicating that the cultural impact on M&A performance depends on the measures examined and also likely to depend on the nature and extent of cultural differences, the integration approach taken & the interventions chosen to manage cultural differences.

Taco H Reus and Bruce T Lamont (2009), aimed to understand the role of cultural distance in international acquisitions through its effects on the development & application capabilities (in terms of understandibilty, communicability & key employee retention). The study has revealed mixed results. On one hand, cultural distance impeded understandibilty of key capabilities that need to be transferred & restricts communication between acquirers and their acquired units, thus bringing a negative impact on acquisition performance. On the other hand, it enriched acquisitions by overcoming these impeding effects and enhancing synergistic benefits. However, the effect of cultural distance on key employee retention was found neutral.

Hema Bajaj (2009), examined the role played by the cultural factors in M&A's by studying the acquisition of old private sector bank (OPSB) by new private sector bank (NPSB) during the period 2003-2004. It was found that culture played a very significant role in M&A's. Despite this fact, cultural similarities/dissimilarities were not taken into consideration before the decision of acquisition was taken. The study also revealed that the two banks had huge cultural differences; threat of cultural conflict was very high. OPSB was well aware about the banking rules and regulations while as NPSB focused much on sales and marketing. OPSB followed a centralised system of communication while as NPSB followed a decentralised one. These cultural differences had a negative impact on the overall productivity after the acquisition took place.

PieroMorosini, Scott Shane and Harbir Singh (1998), examined the effect of national cultural distance on cross-border acquisition performance during the period 1987 to 1992. They examined 52 cross-border acquisitions in which one of the firms was an Italian corporation, and the other was headquartered either in Europe or the United States and found a positive association between national cultural distance and cross-border acquisition performance. It was found that when companies entered culturally distant countries through acquisition, they performed well compared to that acquisitions that were in culturally close countries. The cross-border acquisitions that performed better were those in which the routines of the target firm, such as inventiveness, innovation, entrepreneurship, and decision-making practices were, on an average more distant than those of the acquirer's, providing a mechanism for firms to access these diverse routines which in turn, enhanced the combined firm's performance over time.

Lodorfos, G., and Boateng, A. (2006), examined the role of culture in the merger and acquisition process in the European chemical industry.The study found that cultural differences acted as a key element affecting effectiveness of the integration process and consequently the success of M&A's. The cultural fit constituted a key factor in M&A success and should be given the necessary attention at all stages of M&A's. It was concluded that proper planning with culture being placed at the heart of integration strategies and implementation and the creation of a positive atmosphere for the change- before initiating any actual consolidation of human and physical assets were likely to contribute to merger and acquisition success and value creation.

Deepak K. Datta and George Puia (1995), examined the impact of cultural distance on wealth effects. They studied 112 large cross-border acquisitions undertaken by U.S. firms between 1978 and 1990 and has found that cultural fit does have an important impact on post-acquisition performance. Cultural differences resulted in an inadequate understanding of the foreign firm, causing the acquiring firm to overpay for the acquisition. Acquisitions, thus characterized by high cultural distance were accompanied by lower wealth effects for acquiring firm shareholders.

Conclusion

The relationship between cultural differences and M&A performance is more complex than it appears. Cultural differences have substantial impacts on multiple aspects of merger and acquisition deals.While majority of the studies found national or organizational cultural differences to be negatively related to different measures performance, others found cultural differences to be unrelated or even positively related to the success of M&A's. By critically evaluating various authors' views in the literature of mergers and acquisitions,the results have revealed that inappropriate communication,improper management of cultural integration, and improper acculturation process among the combining entities is the root cause for the failure of a large number of mergers and acquisitions. It is crucial before that before the first contact between the two organizations, each of them prepares themselves to the next big step. Gathering information from their future partners and developing trust through one-to-one interaction between members of both the companies is highly recommended. Conductingcultural assessment of each group to identify various cultural gaps,clarifying doubts through workshops, discovering the degree of commonality and the potential disconnects between the twoand leveraging the best of each group to grow an even better culture will make it easier for managers in creating cultural awareness and building an even better organisation by further facilitating the process of cultural integration.

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