Chapter 2: Review of Related Literature

The literature review chapter on Mergers and Acquisitions is divided into four primary sections viz. (a) Mergers and Acquisitions- a general introduction (b) Mergers and acquisitions- performance and failure (c) Role of HR in post-merger integration d) Best practices or models in post-merger integration.

2.1 Mergers and Acquisitions- a general introduction

This section is divided into three parts. The first part gives an insight into the history of mergers and acquisitions. It also tries to explore and define the conceptual framework of M&As and other related concepts. The second part discusses the motives behind mergers and acquisitions while the final part presents the merger and acquisition classifications with rationale.

2.1.1 (a) History of Mergers and Acquisitions

Mergers and acquisitions are now commonplace as companies try to improve their competitive position in a global market place. Mergers and acquisitions constitute one of the most attractive business strategies that are increasingly adopted and utilized among organisations today. Javidan et al. (2004) defined mergers as a process of combination of the assets, cultural values, and management practices of two separate organisations to form a new entity. In contrast, acquisition, which is widely known as a business takeover, is the process of buying out another business (Daniel & Metcalf, 2001). The core external factors driving the phenomenon of the mergers and acquisitions are global economy, advanced technology, specific market forces and government regulations (Schmidt, 2002). We further define mergers, acquisitions, amalgamations and takeover with certain examples:-
**Merger:** Merger is defined as a circumstance in which the assets and liabilities of a company (merging company) are vested in another company (the merged company). The merging entity loses its identity and its shareholders become shareholders of the merged company. (Desai, 2010)\(^27\)

Merger is referred to as a combination of two or more companies which may involve absorption or consolidation. (Patankar & Chavan, 2011)

In a merger process, two or more organisations come together to meet some strategic objective. They may merge only part of their operation and systems or they may completely merge with each other to develop a new identity.

Thus it is the combination of two or more companies into a single company where one survives and the others lose their corporate existence. The survivor acquires the assets as well as the liabilities of the merged company or companies.

**Acquisitions:** A corporate action in which a company buys most, if not all, of the target company's ownership stakes in order to assume control of the target firm. Acquisitions are often made as part of a company's growth strategy whereby it is more beneficial to take over an existing firm's operations and niche compared to expanding on its own.\(^28\) Acquisitions may be friendly or hostile depending on a company’s willingness to be acquired. (Desai, 2010)\(^29\)

In the context of the business combination, an acquisition is the purchase by one company of a controlling interest in the share capital of another existing company. The acquiring company will remain in business and the acquired company will be integrated into the acquiring company and thus the acquired company ceases to exist after the merger. Some prominent examples of

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\(^28\) http://www.investopedia.com/terms/a/acquisition.asp#ixzz2lm3g69Cv, accessed on 6 Jan, 2012.

acquisitions in India include Hindalco acquiring Canada based Novelis, Dr. Reddy's Labs acquiring Betapharm, Suzlon Energy acquiring Hansen Group and the acquisition of Daewoo Electronics Corp. by Videocon.

In short, a merger is when one company is combined with and totally absorbs another. An acquisition is the process used to transfer assets from company to the other. Acquisition refers to the corporate buy- out of a controlling interest in another organisation or business takeover. Generally, acquisitions can occur in both friendly and hostile environments.

**Amalgamation:** An amalgamation is an arrangement, whereby the assets and liabilities of two or more companies (amalgamating companies) become vested in another company (the amalgamated company). The amalgamating companies all lose their identity and emerge as the amalgamated company; though in certain transaction structures the amalgamated company may or may not be one of the original companies. The shareholders of the amalgamating companies become shareholders of the amalgamated company. (Desai, 2010)

**Takeover:** A takeover generally involves the acquisition of a certain stake in the equity capital of a company, which enables the acquirer to exercise control over the affairs of the company. Unlike a merger or purchase of a division, a take-over does not involve transfer of assets and liabilities. (Patankar & Chavan, 2011)

Takeover is a market route for the acquisition of a company. If management of a prospective selling company is unwilling to negotiate a transaction with a prospective buyer, the buyer attempts to accomplish the acquisition by a takeover bid, offering to buy shares of the seller directly from the shareholders of the seller.

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30 Ibid
2.1.1 (b) Merger Waves

The economic history has been divided into merger waves based on the merger activities in the business world. Mergers have typically followed cyclical patterns beginning with periods of intense merger activity followed by intervening periods of fewer mergers. Historians and M&A specialists have identified the following six merger waves in the history of the United States.

First Wave 1893 – 1904: Horizontal Mergers

The first peak of the first merger wave was reached during a period of economic expansion right after the depression of 1883; between 1898 and 1902. This wave involved mainly the major mining and manufacturing industries but also 15% of all manufacturing assets and workers (Gaughan, 2007). The first wave was one of major horizontal mergers, creating the principal steel, telephone, oil, mining, railroad and other giants of the manufacturing and transportation industries in the United States (US). This wave ended due to the start of World War I.

Second Wave (1916- 1929): Increasing Concentration

The activity during this period was a result of the entry of the United States into World War I and the post-war economic boom. Mergers also tended to be horizontal and further increased industry concentration. The second wave of mergers was most noteworthy in case of major automobile manufacturers. The automaker Ford was integrated from finished car backs to steel mills, rail roads to iron and coal mines. (Lipton, 2006). The stock market crash of 1929, along with passage of the Clayton Antitrust Act that further defined monopolistic practices, brought this era to a close. (DePamphilis, 2012)
Third Wave (1965-1969): The Conglomerate Era

This period of M&A activity was characterized by the emergence of financial engineering and conglomerate. A rising stock market and the longest period of uninterrupted growth in U.S. history to that time resulted in record price-to-earnings (P/E) ratios. Companies given high P/E ratios by investors learned how to grow earnings per share (EPS) through acquisition, rather than through reinvestment. Companies with high P/E ratios would often acquire firms with lower P/E ratios and increase the EPS of the combined companies, which in turn boosted the share price of the combined companies; so long as the P/E applied to the stock price of the combined companies did not fall below the P/E of the acquiring company before the transaction. To maintain this pyramiding effect, though, target companies had to have earnings growth rates sufficiently attractive to convince investors to apply the higher multiple of the acquiring company to the combined companies.


The 1980s, a decade that saw the rise of the corporate raider, were characterized by the breakup of many major conglomerates and a proliferation of financial buyers using the hostile takeover (rarely used previously) and the leveraged buyout (LBO) as their primary acquisition strategies. The first major hostile bid was witnessed in 1980 when Morgan Stanley on behalf of Inco (the same Inco that had been involved in the four-way takeover struggle that ended with its takeover by Vale) was seeking to take over ESB. (Lipton, 2006)

Management buyouts and takeovers of U.S. companies by foreign acquirers became more common. Conglomerates began to divest unrelated acquisitions made in the 1960s and early 1970s. In fact out of the acquisitions made outside the acquirer's main line of business, some 60 percent had been sold out by 1989.

Although M&A activity did diminish during the 1990 recession, the number of transactions and the dollar volume rebounded sharply in the beginning of 1992. This was the age of strategic mega merger or the fifth wave period.

During the fifth wave, companies of unprecedented size and global sweeps were created on the premise that size was all that mattered and with the imminent stock market boom. Companies, during this period, lured and pressured by the high stock prices signed deals to maintain heady trading multiples (Lipton, 2006).

The longest economic expansion and stock market boom in U.S. history, uninterrupted by recession, was powered by a combination of the information technology revolution, continued deregulation, reductions in trade barriers, and the global trend toward privatization. Both the dollar volume and number of transactions continued to set records through the end of the 1990s before contracting sharply when the Internet bubble burst, a recession hit the United States in 2001, and global growth weakened. The fifth wave of mergers and acquisition saw its end with the burst of the millennium bubble and scandals like that of Enron. (Lipton, 2006)\(^{31}\)

Sixth Wave (2003-2007): The Rebirth of Leverage

US financial markets during the sixth wave, especially from 2005 through 2007, were characterized by an explosion of highly leveraged buyouts and private equity investments (i.e., takeovers financed by limited partnerships) and the proliferation of complex securities collateralized by pools of debt and loan obligations of varying levels of risk. Much of the financing of these transactions, as well as mortgage-backed security issues, took the form of

\(^{31}\)ibid
syndicated debt (i.e., debt purchased by underwriters for resale to the investing public).

Some of the principal factors that triggered the sixth wave included globalization, support from governments in countries like France, Italy and Russia, rise in commodity prices, availability of low interest financing, hedge fund and other shareholder policy. (Lipton, 2006)

2.1.1 (c) Theories of Mergers and Acquisitions

The four different schools of thoughts (Haseslagh and Jemison 1991) have been discussed, each of which has its own objective:

1. The capital markets school: The capital markets school is concerned with the question to find for whom is the value created from mergers and acquisitions. It basically studies the impact of acquisitions on wealth creation at a societal level. It also examines agency issues, the role of investors, and public vs. private firms. (Goldberg 1983, Ravenscraft and Scherer 1987).

2. The strategic management school: The strategic management school focuses largely on the diversification strategy and how related and unrelated acquisitions perform relative to each other. The objective is to relate to the performance of the acquiring and the acquired firm. Healy, Palepu and Ruback (1997) found in some strategic circumstances (friendly, stock-based purchase of a related business) returns were positive while hostile, non-strategic deals did no better than break even. In another study, Morosini, Shane and Singh (1998) used growth rate in sales to assess M&A performance but it was unclear whether increase in sales was necessarily reflective of successful integration.
3. The Organisational behaviour school: The organisational behaviour school focuses its attention on the behavioural implications of acquisitions, at both the individual and organisational levels. The organisational behaviour of acquisition research comes from basically two major directions: how people respond to acquisition situations and how acquisitions impact on the organisation and the people in it. The primary focus in the first instance comes from a psychological perspective i.e. an acquisition is a traumatic transformational event for people in organisations creating a sense of loss, lack of trust, stress, uncertainty, and the associated resulting behavioural problems (e.g. Buono and Bowditch, 1989; Marks and Mirvis, 1985 and 2001; Harris and Sutton, 1986; Buono, Bowditch, and Lewis, 1985; Schweiger and Walsh, 1990). Napier (1989) provides a good review of HR issues in mergers and acquisitions from an organisational behavioural perspective.

4. Process Perspective: Process perspective is focussed on the actions taken by the management to guide the post-acquisition integration process. The potential benefits and the synergies entirely depend upon the management’s efforts to manage the post-acquisition process in an effective manner (Hunt 1990, Shrivastava 1986).

While there is a concern for post-acquisition integration in process and the organisational behaviour perspectives, the two schools of thought differ substantially in their objective function. The former views value creation (or task integration) as the objective of the acquisition, measured in terms of transfers of capabilities and resource sharing; the latter is concerned primarily with generating satisfaction, and ultimately a shared identity, among the employees from both companies process, which can be called as human integration(Birkinshaw, Bresma, Hakanson, 2000). These concepts have been discussed later in the literature.
2.1.2 Motives of Mergers and Acquisitions

Motives of Mergers and Acquisitions

There are various motives for acquisitions and mergers. These extend from economies of scale to managerial motives. An attempt has been made to evaluate some of these reasons. While one often hears CEOs saying that M&As are inspired by a desire to diversify or achieve higher growth rate, the reasons could be varied. Some of the commonly identified reasons are as follows (Haspeslagh and Jemison, 1991):

1. Inefficient Management: Inefficient management provides a rationale for conglomerate mergers. The management in control is not able to manage assets effectively. Merger with another firm can provide the necessary supply of managerial capabilities. Thus takeover is seen as an effort by the shareholders of the acquired company to discipline the management of the company. The shareholders of the target company through the takeover, pass on the control to the more efficient management. The price paid to the shareholders has to be at a premium over current market price to solicit them to sell their shares. (Jensen and Ruback, 1983)

2. Synergy: Synergy is based on the notion that merger of two companies can create greater shareholder value than if they are operated separately. The two types of synergy are operating synergy and financial synergy. Operating efficiency is improved by economies of scale or economies of scope. Economies of scale refer to the reduction of average cost with increase in volume. They can be important in any business with substantial fixed overhead expenses such as steel, pharmaceutical, chemical and aircraft manufacturing. They may be realized when the merging companies are in the same line of business. Such horizontal mergers eliminate duplication and concentrate a greater volume of activity into a given facility. Economies of
scope refer to using a specific set of skills or an asset currently employed in producing a specific product or service to produce related products or services. When HUL acquired Lakme, it helped HUL to enter the cosmetics market through an established brand. When Glaxo and Smithkline Beecham merged, they not only gained market share, but also eliminated competition between each other (Aurora, R. et al, 2011).

3. **Diversification:** Diversification, or acquiring a different line of business, is sometimes a motive for mergers. Such mergers reduce the instability of earnings. If the two firms have cash flows that are unrelated their combined cash flow may be less volatile than their cash flows viewed separately. Investors may require a lower rate of return to invest in the combined firms securities referred to as coinsurance. But the impact on share price depends on whether investors are able to diversify their portfolio efficiently. Investors evaluate risk in an overall market context, not just in terms of total risk of the firm. However, diversification by reducing relative variability of cash flows, benefits debt holders in having a more credit worthy claim. Diversification is also undertaken to shift from the acquiring company's core product lines or markets into those that have higher growth prospects. (Amihud and Lev, 1981)

4. **Agency Problems:** -Takeovers would be a threat because of inefficiency or agency problems. Mergers take place to correct situations where there is a divergence between the goals of management and owners. For example we have the case of a management that owns a small fraction of shares, pursues its own goals such as a lavish life style and the cost of mismanagement is spread across a large number of shareholders. Low stock prices of such firms attract acquirers who perceive the share to be undervalued. Management of such firms is forced out to raise share price. (H.R. Machiraju2003, Roll 1986)
5. **Tax Considerations:** Unused net operating losses of the target company and their valuation or write-up of acquired assets and the tax free status of the deal influence M&As. If a healthy company acquires a sick one, it can avail of income tax benefits under section 72-A of income tax Act. This stipulates that subject to the merger fulfilling certain conditions, the healthy company’s profit can be set off against the accumulated losses of sick unit. The money saved must be used for the revival of the sick unit. Losses carry forward and can be set off against the combined firm’s taxable income. The seller considers the tax free status as a prerequisite to the deal. Otherwise he may want a higher price to meet the tax liability (H.R. Machiraju, 2003).

6. **Market Expansion:** Organic root of growth takes time. Organisations need place, people, regulatory approval and other resources to expand in to newer product categories of geographical territories. Acquisition of another organisation with complementary product of geographic spread provides all these resources in a much shorter time, enabling faster growth. Merger of Orange, Hutch, and Vodafone took place to achieve this objective. (Aurora, R. et al, 2011)

7. **Purchase of Assets below their replacement costs:** Sometimes a firm will be touted as an acquisition candidate because the cost of replacement of its assets is considerably higher than its market value. For eg. Earlier in the 1980s the oil companies could acquire reserves at a cheaper cost by acquiring other oil companies than by doing exploratory drilling (H.R. Machiraju, 2003).

8. **Manager’s Personal Incentives:** Many a times, business decisions are based on manager’s personal motivation than on economic analysis. Business leaders like power and more power is associated with running a larger corporation than a smaller one. No executive would admit that his/her ego was the primary reason, but egos do play a role in many mergers. Executive
salaries are highly correlated with company size- the bigger the company, higher the salary of the top officials.

2.1.3 Merger and Acquisition Classifications

The M&A process itself is a multifaceted one which depends upon the type of merging companies. A review of the literature highlighted historical perspective consistent with the merger and acquisition waves. The four kinds of mergers and acquisitions which have been studied are:-

**Horizontal Merger:** Horizontal mergers occur when two firms in the same market are consolidated into a single enterprise (Jones T, 2004). Over the years, most mergers have been horizontal combinations in which the acquiring firm increased its share of a market either by increasing it market share in a given geographic area or by expanding into new areas. Until recently, the conventional wisdom was that the economic motivation for horizontal mergers was the increased profit to be realized through gaining power over prices and quantities by reducing competition. But it is now recognized that another rationale for horizontal combinations is the lower cost and higher productivity that result from the realization of economies of scale and scope (Lutzeler P. M., 1994). Horizontal mergers often characterize industries and markets whose products are generally in the mature or declining stages of the product life cycle. The overall growth of these markets is low and the firms have built up production capacity that far exceeds the demand (Sudarsanam S, 2003).

A horizontal merger of two firms in the same market increases the market share of those firms conferring enhanced market power to dictate the output price or to compete more effectively on non-price terms. When the merger results in enhanced market power for the merging firms through a large
increase in market share and price elasticity of their products is unchanged, the firms may also increase their revenue. Horizontal mergers require the highest degree of integration (Srivastava, 1986)

**Vertical Merger:** Vertical merger is between two companies producing different goods or services for one specific finished product. A vertical merger occurs when two or more firms, operating at different levels within an industry's supply chain, merge operations. Most often the logic behind the merger is to increase synergies created by merging firms that would be more efficient operating as one (Investopedia).³²

The basic objective of a vertical merger is to eliminate costs of searching for vendors, contracting prices, payment collection, advertising, communication, and coordinating production. Such a merger can have a very positive impact on production and inventory since information flows efficiently within the organisation. (Smart W. L. , 2009). It is to be noted that vertical mergers need to be timed appropriately. History shows that vertical mergers occur when two firms decide to integrate their businesses to capitalize on the rising demand for their products. In vertical mergers, the scope for market power enhancement is bleak. Since the end product of the vertical chain will remain the same, it is the ownership and the organisation of intermediate stages of production or distribution that get reshuffled through vertical integration, the scope for real options and breakthrough remain quite limited (Sudarsanam S, 2003).

**Conglomerate Merger:** A merger between firms that are involved in totally unrelated business activities are conglomerate mergers. There are two types of conglomerate mergers: pure and mixed. Pure conglomerate mergers involve

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firms with nothing in common, while mixed conglomerate mergers involve firms that are looking for product extensions or market extensions.\(^{33}\)

There are many reasons for firms to want to merge, which include increasing market share, synergy and cross selling. Firms also merge to diversify and reduce their risk exposure. However, if a conglomerate becomes too large as a result of acquisitions, the performance of the entire firm can suffer. This was seen during the conglomerate merger phase of the 1960s. In the early 1980s, researchers also theorized that managers pursue conglomerate mergers for risk reduction motives that were personal instead of corporate. Managers are motivated to pursue conglomerate mergers in order to reduce their employment risk. (Smart W. L., 2009).

2.2 Mergers and Acquisitions – Performance and Failure

2.2.1 Mergers and Acquisitions- performance evaluation

Evidence regarding the effects of mergers as success or failure comes to us from many different sources. Much of the evidence comes from the finance literature. The main focus is on the ultimate effect of a merger on the stockholders of the acquiring and target company, and on the market share, productivity, profits or price-cost margins. According to Paul (2001): “one common technique for examining the effects of a merger or acquisition employs the stock market's reaction to the event.”


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Bradley, Desai and Kim (1983) found that target firm stockholders realize significant positive abnormal returns upon the announcement of a takeover offer even if the takeover does not go through. The authors concluded that these gains are primarily due to stock market anticipation of a future successful acquisition.

Rather than using abnormal stock market price movements around the time of an event as predictors of future actual performance, certain researchers have examined the market performance of merging companies over a long period of time (a few months to a few years).

In many of the cases it is been seen that the intended benefits of acquisitions are often not realised over a period of time: Moeller, Schlingemann, and Stulz (2004) analyzed the performance of acquiring companies through the two major merger waves that occurred during that time period. They found that over a period of 1998 to 2001 shareholders in bidders lost $240 billion.

Dodd (1980) in his study found that the stockholders of target firms earned large positive abnormal returns from the announcement of merger proposals i.e. approximately 13 % at the announcement of the offer and 33.96 % over the duration of the merger proposal (10 days before and 10 days of the announcement). But the stockholders of bidder firms in both completed and cancelled merger proposals experienced negative abnormal return of -7.22% and -5.50%, over a period of time.

Research studies done by Ravenscraft and Pascoe 1989 and Kaplan 1993 each have found a weak correlation between the stock markets and the profitability or the cash flows of the merged company in the long run. About half of all M&As create value; the other half do not. Mergers, on an average, fail to realize potential gains that are thought to exist at the time of the announcement (Dalton, Daily, and Covin2004).
Consistent with poor merger and acquisition performance, a study by McKinsey & Company found that only 23% of mergers and acquisitions succeeded. 60% of the mergers and acquisitions in the study failed and did not produce sufficient returns necessary to even finance the corporate combinations. Related studies indicated that up to 45% of these acquired companies eventually sold or became restructured stand-alone business entities (Hitt et al., 2001).

Sirower (1997) studied 28 financial performance factors. He found that acquisitions not only reduced the acquiring firm’s value in the due course but acquisitions premiums adversely affected performance of the acquiring firm. Further multiple bidders negatively impacted acquisition performance.

When executives are asked to rate the transactions in which they are personally involved, most respond that their deals create value and that their firm’s strategic goals are achieved. In contrast, majority of executives tend to respond that only 20 to 30 percent of all M&As in general either create value for acquiring firms or achieve the firm’s strategic objectives (Baker, Miller, and Ramsperger, 1981).

The corporate leadership council M&A survey (2006) revealed that 12% of organisations report significant success in M&A, while 34% report no success in M&A transaction. Furthermore 77% of M&A do not achieve their original purpose. 50 to 80% of mergers and acquisitions never produce anticipated benefits.

The paper by Kumar (2009) examined the post-merger operating performance synergies of acquiring companies during the period 1999-2002 in India. It was found that the post-merger profitability, assets turnover and solvency of the acquiring companies, on average, showed no improvement when compared with pre-merger values. It was seen that the acquirer’s industry adjusted profitability declined from the third year of acquisition. Results also indicated
that the post-merger operating efficiency of companies, on average, was lower than that of the industry average. Thus the merger decisions sometimes are not aimed at maximizing profits and hence the wealth of shareholders.

Every merger, acquisition, or strategic alliance promises to create value from some kind of synergy, yet statistics show that the benefits that look so good on paper often do not materialize (Rosalind and Kirstie 2004). The question thus is now triggered - what causes such failures as mergers aren’t really successful nor do they realise value or synergy.

The next section highlights the reasons for failure in mergers and acquisitions. It highlights the neglect of HR issues especially at the integration stage.

2.2.2 Reasons of Merger failures

M&A failure has been attributed to many reasons: imitation of other M&A strategies without proper understanding (Haunschild, 1993), lack of integration (Haspeslagh & Jemison, 1991; Nahavandi & Malekzadeh, 1988; Weber, 1996), managerial hubris (Haunschild, 1993; O’Neill, Pouder, & Buchholtz, 1998), inadequate estimation of target, lack of commitment, lack of leadership or strategic guidance after the negotiations of M&As.

Allred et al. (2005) found in his studies that impact of mergers and acquisitions is also due to the unequal sizes of mergers. If the companies merged or acquired are of different sizes, there would be power imbalance especially if the acquired is of a smaller size.

Gadiesh and Ormiston (2002) has discussed five possible reasons for the failure of a merger – poor strategic rationale, overpayment for the acquisition, inadequate integration planning and execution, a void in executive leadership and cultural mismatch.
Using questionnaire & interviews from British case studies, Haspeaslagh and Jeminson (2004) in their research across twenty companies have drawn together the HR issues elements from entire spectrum of merger literature. They argue that acquisition managers choose to focus on quantifiable financial issues and ignore the messy human dimension. As a result, manager over simplify key issues and fail to develop creative HR solutions.

A number of authors have listed down a multitude of reasons which causes merger failure. One of the common reason which has been discussed by many researchers over a period of time is the non involement or late involvement of HR professionals in mergers and acquisitions (Ajjarapu, 2004; Daniel & Metcalf, 2001; Giles, 2000; McIntyre, 2004; Ruth, 2000)

A study done by Dixon and Nelson (2005) found that the HR professionals were not included in the mergers and acquisitions team. The team only comprised of employees from the finance, IT and other disciplines. Organisations while deciding to merge or acquire look into the financial and legal aspects, but they somehow fail to look into the human resources aspect of the organisations.

Many organisations, though now more concerned about ‘softer’ issues, still overlook HR side of integration, at least in the initial stage of the merger process. Lack of direct involvement of HR during the strategic decision making and pre-merger phase is one of the main reasons for a merger going sour. Harman and Greengard (1999) in their research reported that 80% of combinations failed at the implementation stage as a result of senior HR professionals brought in too late. In a research done by Giles (2000) and it was found that that only 35% of senior HR executives were involved in M&A activities.

The research paper by Bjorkman (2006) who interviewed 60 HR managers and top executives in Nordea found no evidence of the HR playing a role as
employee champions, strategic partners or change agents as desirable. It is left with a secondary non-strategic role in these processes. This could be attributed to a perspective of the top management that HR has no/minor role to play as far as strategic decisions are concerned.

Thus apart from non-involvement of HR in the planning stage, research has shown that many HR professionals either are not involved in mergers and acquisitions or left with a non-strategic role.

Reasons for merger and acquisition failures were also a topic of performance-based research. Kode et al. (2003) conducted a comprehensive examination of existing literature in this area. Tab. 2.1 provides an overview of their findings.

Literature study done by Kode et al. (2003) examined different reasons for merger and acquisition failures. ‘No plan to integrate and integration problems’ in column 1 appeared to be amongst the highest along with ‘payment of too high an acquisition premium’. This was cited by eleven researchers out of a total of fifteen. The first and fourth content columns directly related to merger and acquisition integrations. ‘Synergy and value’ addressed in the third and sixth content columns were also functions of the integration process. ‘Integration related considerations’ surfaced in four of the seven categories as primary reasons for merger and acquisition failure. As a function of the total number of studies examined, 14 of 17 (82.4%) cited business combination failures related to post-merger and post-acquisition integration (Kode et al., 2003).

Out of the three factors price, strategic management and post-merger integration studied by Smith (1997) handling integration management was the most important factor which determines the success or failure in an M&A.
Tab. 2.1 Reasons for merger and acquisition failure

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<th>Failure to understand the acquisition game formulae</th>
<th>Biases in favour of synergies and its consequences</th>
<th>Slow pace of integration</th>
<th>Inadequate due-diligence, no strategy, poor preparation and undue haste</th>
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<td>Rappaport (1998)</td>
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<td>Seyhun (1990)</td>
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<td>Sirower (1997)</td>
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<td>Sweig (1995)</td>
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<td>Frequency (out of a total 15)</td>
<td>11</td>
<td>2</td>
<td>4</td>
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<td>6</td>
<td>3</td>
<td>11</td>
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A lot of existing literature on the impact of mergers and acquisitions has examined the post-merger and acquisition integration issue (Kode et al., 2003, Pritchett et al., 1997, Smith, 1997), and neglect of HR function in mergers and acquisition. The role of HR today has become very critical in all areas. With deals worth $ 43.4 billion of mergers and acquisitions in India alone in 2012, the need for early involvement of HR in the deal and the need for strategic consideration of people issues have been heightened. What has not surfaced so far is the importance of the role of HR professionals in mergers and acquisitions.

According to Anderson (1999) if the HR is involved at the pre-merger discussion and at the strategic planning phase, the HR can identify the areas of divergence of both the companies which could hinder the integration. Indeed, human resource development often becomes a critical factor that influences the success in mergers and acquisitions (Daniel & Metcalf, 2001; Jeris et al., 2002).

Gaughan (2005) stated: “Human resource departments in today’s organisations are practical and strategic. As such, they can add significant value for companies through development, managing personnel conflict, reinforcing the new HR system and corporate culture, and providing leadership and communication to reduce turnover.

Cartwright and Cooper (2000) acknowledge the leading role of modern human resources functions and believe it should be actively involved in the organisation and perform as a business partner and as an advisor on strategic and business-related issues.

The above section of the literature has highlighted the failure in mergers and acquisitions. It is evident that that one of the main causes of failure in mergers and acquisition is the ignorance of people issues and the non-involvement of

34 Online edition of The Economic Times, Reuters, January 4, 2013
HR role. The next section would discuss the role of HR in different stages of mergers and acquisitions, specifically focussing on the integration stage. It would highlight the types of integrations and the different schools of thought. It would also review the outcomes of a mergers and interventions used by the HR professionals.

2.2.3 Stages in Mergers and Acquisitions

Traditionally, the cycles of mergers and acquisitions are comprised of three stages: pre-merger and acquisition stage, due diligence stage and post-merger integration stage (Daniel & Metcalf, 2001; Hitt & Pisano, 2004; Jeris et al, 2002).

1. Pre-merger and acquisition stage: The pre-merger and acquisition stage begins with a screening process based on the criteria for selection of a potential target organisation for merging or acquiring.

The pre-merger stage is an extensive decision-making, planning and positioning process. The decision to acquire or to merge is typically made by a few executives only, or sometimes even by a single chairman or CEO. After the decision on principle, the first step is the screening of potential targets and the drawing up of a ‘hit list’ of identified potential companies. The two most important criteria of selection mentioned in the literature are (a) projected earning potential and (b) strategic fit in terms of products, markets, geographical location and so on (Cartwright and Cooper, 1990; Hunt, 1988; Picot, 2002). Thus the decision to merge is purely based on economic and financial considerations while the ‘true’ psychological reasons are often masked.

The failure of mergers and acquisitions can be seen to occur when an organisation makes a wrong choice in selecting the target organisation to
merge with or acquire, resulting in incompatibility of cultural values, clashes in management practice, and loss of key talent (Schmidt & Lafaix, 2002).

Since people problems are a primary source of poor M&A performance, involving HR managers early in the decision-making process is an important part of any M&A strategy (Marls and Mirvis 1986; Marks and Cutcliffe 1988). According to Tower Perrin, analysis and research conducted by the Society of Human Resource Management (2002), the involvement of HR professionals in the pre-merger and acquisition stage would avoid merger failures.

2. Due diligence stage: Due diligence is the process of planning and validating the agreement between the two organisations to be combined. Giffin (2002) suggested that the due diligence process is comprised of multiple purposes. Some of them include including the following: Planning and verifying to resolve issues in the merger and acquisition deals; meeting the expectations of the two organisations to be combined; analyzing organisation issues and people issues between the two organisations to be combined, including employment retention and cultural compatibility; and planning change in the management process for the integration stage.

However, the primary focus of the human resource development aspect during the due diligence stage is analysing and planning for resolution of organisation issues and people issues. (Schmidt, 2002). Indeed, human resource development professionals should carefully analyze and validate issues of compatibility to determine how the new entity’s key employees will respond to significant changes during the merger and acquisition process (Javidan, 2004).

According to Greengard (1999) cultural issues can determine whether a deal will work or break. Thus developing a cultural audit tool and detailed checklist can guide organisations through the due diligence process. The HR department should be co-opted as a strategic participant in the entire process.
3. **Post-merger integration stage:** The post-merger integration stage can be viewed as a systematic process of planned change and development. The integration stage is focused on change and integration in the organisation’s system, structure and management practices. In addition, the integration stage includes redesigning work processes to assign new roles and authority to employees (Cianni, 2002; Hitt et al., 2004).

Empirical studies have shown that the speed of integration can become a critical factor determining the success of mergers and acquisitions (Daniel and Metcalf, 2001; Schmidt, 2002). Delay in the integration process can create unnecessary ambiguity, employee anxiety, and uncertainty throughout the organisation (Daniel & Metcalf, 2001; Horwitz et al., 2002). Moreover, Davenport (2002) stated that the integration stage has been recognized by HR scholars and practitioners to be the most important stage among the different stages of the merger and acquisition process because the different cultural values, management practices, organisation policies and work processes of the two companies need to be integrated and combined to achieve the merger and acquisition goals.

Cianni (2002) suggested that the integration process should focus on the organisation structure, processes, policies, people and culture. In addition, integration plans should focus on the performance management system and compensation programs, including performance appraisals, executive compensation, benefits, retirement, a health and welfare plan, and bonuses and other incentives (Daniel & Metcalf, 2001; Schmidt, 2002). HR programs in training and development are particularly important for improving employee performance and ensuring that employees will have the competencies required for future jobs (Jacobs, 1989; Swanson & Holton, 2001).
Moreover, Cianne (2002) suggested that the organisational issues should focus on the processes of integration of human capital and change management during the merger and acquisition process. In fact, the change management process involves a new design for the entire combined entity and focuses on organisation structures, organisation systems, and management practice and policy.

2.2.4 Integration

In this section the highlight is on the post merger and acquisition integration stage which is the main focus of the study. It discusses the different schools of thoughts in the integration process. The literature also provides with a wide number of issues arising in the integration stage and its outcomes. It highlights the different HR interventions used by the HR professionals and employee satisfaction on the same.

2.2.4 (a) Post-Merger and Post-Acquisition Integration Process

According to some researchers post-acquisition integration occurs after the official change of control. Some argue that integration begins during the due diligence phase (Hickins, 1999). The argument is supported by the position that it is during the initial due diligence period when leaders of both the organisations begin to explore the similarities and differences of each other’s respective organisational cultures (Bijisma-Frankema, 2001). For the acquired employees the integration process actually begins immediately after the official change of control date (Cartwright & Cooper, 1996)

Integration

Integration refers to the managerial actions taken to combine two previously separate firms and is a key determinant of acquisition performance
(Larsson and Lubatkin, 2001). The objective of the integration stage is to bring out the synergies and benefits anticipated at the planning stage (Karim, 2006).

Integration is defined in general terms as the process of combining two companies into one entity at every level. Integration involves the synthesis of people into one corporate culture. The new culture may simply be the culture of the acquiring company that is superimposed on the acquired company or some new entity that is a combination of the best aspects of both corporate cultures. Integration is also the combining of the two companies’ systems into one set. (Birkinshaw et al. 2000).

However an important area of focus here is to what extent an organisation wants to integrate the two companies’ systems into one set. Over or under integration can result in a failure to create value. (Amy L Pablo 1994) Thus level of integration is very critical.

According to Amy L Pablo (1994), level of integration can be defined as the degree of post-acquisition change in an organisation's technical, administrative, and cultural configuration. Level of integration is an important concept in acquisition management because, although high levels of integration theoretically enhance realization of interdependency-based synergistic potential, they may also result in realization of negative synergies as a result of increased coordination costs and potential for inter-organisational conflict.

A low level of integration is conceptualized as one in which technical and administrative changes are limited to the sharing of financial risk and resources and the standardization of basic management systems and processes to facilitate communication. A moderate level of integration includes increased alterations in the "value chain" as physical and knowledge-based resources are shared or exchanged. Administrative changes at this level may include selective modifications in reporting relationships and delegation of
authority. The highest level of integration is conceptualized as being quite inclusive, involving the extensive sharing of all types of resources (financial, physical, and human).

The most important question which now arises is “what are the important factors that determine the level of integration post mergers and acquisition” According to Shrivastava (1986) post-merger integration takes place at the procedural, physical and managerial /socio-cultural levels. The following table (Tab. 2.2) shows clearly the co-ordination, control and conflict resolution aspects that the HR needs to handle to manage procedural, physical, managerial and socio-cultural tasks involved in integration.

Tab. 2.2 Post-merger integration tasks

<table>
<thead>
<tr>
<th>Post-Merger Integration Tasks</th>
<th>Coordination</th>
<th>Control</th>
<th>Conflict Resolution</th>
</tr>
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<tbody>
<tr>
<td>Procedural</td>
<td>• Design accounting systems and procedures</td>
<td>• Design management controlling system</td>
<td>• Eliminate contradictory rules and procedures</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>• Rationalize systems</td>
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<tr>
<td>Physical</td>
<td>• Encourage sharing of resources</td>
<td>• Measure and manage the productivity of resources</td>
<td>• Resource allocations</td>
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<td></td>
<td></td>
<td></td>
<td>• Asset redeployment</td>
</tr>
<tr>
<td>Managerial and Socio Cultural</td>
<td>• Establish integrator roles</td>
<td>• Design compensation and reward systems</td>
<td>• Stabilize power sharing</td>
</tr>
<tr>
<td></td>
<td>• Change organisation structure</td>
<td>• Allocate authority and responsibility</td>
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</table>
Similar concepts are given by Birkinshaw et al. (2000) who uses the terms of task integration and human integration. The author has explained how task and human integration has an impact on merger success or failure. The figure below explains the model given by the author.

<table>
<thead>
<tr>
<th>Level of Completion of Human Integration</th>
<th>Level of Completion of Task Integration</th>
<th>Outcome</th>
</tr>
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<tbody>
<tr>
<td>Low</td>
<td>Low</td>
<td>Mixed success: Satisfied employees but no operational synergies achieved</td>
</tr>
<tr>
<td>High</td>
<td>High</td>
<td>Successful acquisition</td>
</tr>
<tr>
<td>Low</td>
<td>High</td>
<td>Failured acquisition</td>
</tr>
<tr>
<td>High</td>
<td>Mixed success: Operational synergies achieved at the expense of employees</td>
<td></td>
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</tbody>
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Fig. 5 Impact of Task and Human Integration processes on acquisition outcome

Task integration is defined as the identification and realization of operational synergies and human integration is defined as the creation of positive attitudes towards the integration among employees.

As indicated in Fig. 5, an emphasis on human integration may result in satisfied employees but no operational synergies, while an emphasis on task integration can lead to the achievement of synergies but with a loss of employee motivation. For the process to be entirely successful both task and human integration has to be effective.
The importance of the post-merger integration is derived from the fact that the value creation can only begin when the organisations begin to work towards the purpose of the acquisition.

Any changes that are designed to capture synergies are implemented in the integration stage. An important part of the post merger integration design decision is whether changes should be made in one or both organisations (Schweiger and Weber, 1989).

Integration involves a complex and interactive mutual adjustment process between the two organisations. However the change is frequently one-sided, occurring primarily within the acquired organisation (Buono & Bowditch, 1989; Datta, 1991; Hambrick & Cannella, 1993; Shanley & Correa, 1992). Studies have shown that an acquired company is often expected to conform to the acquirer’s culture (Chatterjee, Lubatkin, Schweiger, & Weber, 1992), and where changes are made in processes, policies, and plans, those of the acquirer are often used (Schweiger & Walsh, 1990).

The next section would discuss the role of HR in the integration stage and the interventions used by HR.

2.3 Role of HR in the Integration Stage

The role of HR in the integration stage is assimilating employees of the acquired/merging organisations into acquiring/merged entity. According to Bajaj (2007) the role of HR in the integration process includes two sub processes. The first sub process enables integration of people through culture building exercises, communication and facilitation of learning or training on new products, policies and processes. The second sub process enables integration of HR practices and processes through combination of
organisation, reward systems, service conditions and policies of employee relations.

2.3.1 HR issues in integration

Extensive research in post mergers and acquisitions has identified a series of HR issues arising in the integration stage. This section highlights each of these issues-

2.3.1. (a) Structural Issues: Haspeslagh and Jemison (1991) found that post-acquisition management is a strategic process, which involves organisational learning and change, resulting in a new entity which is more than just the sum of the two companies. One of the practical problems faced by the organisation is the difference in the structures of both the organisations. Appelbaum (2000) highlights the importance of making quick organisation structural decisions. It is crucial for both the acquiring and acquired company HR professionals to openly discuss, as a group, and formulate the best organisational structure.

Changes in the structures bring forth certain issues post mergers. New designation, staffing, changes in the reporting relationships of the new organisation with the right people becomes critical.(Haspeslagh and Jemison 1991). Valuable people may be lost because of the wrong designation and staffing decisions without any plan.

The question which lies before the HR professionals here is implementing changes at the right time and the mechanism for the structural changes.

According to Schweiger, Csiszar and Napier 2002, in structural changes, combining of units takes place post-merger which is done to capture the combination of two firms. Combining units means integration of two entities. Schweiger, Csiszar and Napier (2002) have proposed three terms: Assimilation, Novation, and Structural integration. Assimilation occurs when
two units are combined and one unit adopts some or all of the identity of other. Assimilation can be either forced or voluntary. It results into culture clash and resistance to the combination by units in target forms. Novation occurs when two units are combined and new identity is created. It typically involves a combination of developing new cultures and practices. Structural integration occurs when two units are combined, but retain their own identities.

Research has found that the dominant firm often attempts to centralize the control function within the acquired firm; particularly with respect to changing the structures (McCann and Gilkey 1988). According to the authors this approach could create problems in the target company.

Study done by Bohl (1989) found that among companies reporting no post-event problems, 40% had left the management structure unchanged post merger for a period of a year. In organisations where there were no changes in the structure post merger absenteeism and turnover were in control as compared to organisations where there were changes.

J.P. Walsh’s (1988) research on the employment status of top managers for five years from the date of an acquisition indicates that following an acquisition or merger, top management turnover is ‘significantly higher than normal turnover rates’.

In fact, many experts believe that companies can create value from takeovers merely by replacing incumbent management teams with their own, more skilled managers (Kale, Singh, Raman, 2009). The research clearly mentions that decision making i.e. which department will merge, which unit will close down, whom to retain, becomes very important at this stage.

High turnover after an acquisition is more than just a symptom of organisational problems—it may be an important cause. The loss of employees at the outset affects operations directly. It has the indirect effect of
demoralizing a workforce already compromised by downsizing, and perhaps triggers a wave of further executive departures. Thus retaining key talent becomes very critical in the long run. (Jeffrey A. Krug 2003)

It was found that acquiring companies that retain the top executives from the acquired company tend to have more successful outcomes than those that do not (Krishnan, Miller & Judge. 1997). However, it is difficult to retain all acquired company’s top executives, as most are lost within a few years of the acquisition (Krug & Hegarty, 1997; Walsh, 1988, 1989; Walsh & Ellwood, 1991). Retention of acquired company’s top executives is linked positively with post acquisition performance, but many of these executives leave, creating dilemmas about which ones are most valuable to keep and which are not. The acquiring company's top executives also influence the implementation of the acquisition through their organisational knowledge, power, and experience (Haspesiagh & Jemison 1991).

Kiessling, T., & Harvey, M. (2006), examine the impact of retaining top management team post merger. The results showed that there is a positive correlation between the post-acquisition performance of the acquired company and the extent of retention of the top management team in the company post M&A.

Often units are shut down due to non-compatibility of production capacity, product lines, inefficient processes and techniques. Also, depending on the type of merger or acquisition and the amount of integration between the two organisations, duplication of functions is likely to occur. Both the cases result in downsizing. To even out the process of downsizing, employees should be communicated about any downsizing strategies. Sheehy (1988) recommends that HR should be honest about any kind of downsizing activity carried out in the organisation and inform people about what is going to happen in the future.
According to Kay and Shelton (2000), once measures to promote the retention of key employees have been taken, the handling of terminations also should be focused upon. The best long-term strategy is a very generous severance plan; the cost is high, but good plans have a strong positive influence on the morale of the remaining employees.

Firms in mature or declining industries are faced with the challenge of redeploying their excess resources to new applications, and M&A strategies can be an important component of this effort. In redeployment strategy, firms seek attractive opportunities and markets in related industries, using acquisitions to fill any resource deficiencies. In the consolidation strategy, firms combine with their competitors within the same industry. The resulting larger pool of resources provides greater opportunities for disposing off their under-utilized resources through the market, while enhancing their profitability (Jaideep Anand, 2005).

Post downsizing, considerable uncertainty and frustration may be exhibited among remaining employees, who may feel that the termination decisions were based on unclear or inappropriate criteria (Schweiger, Ivancevich, and Power 1987). It has been seen that automatic elimination of redundant positions correlates highly with post-event problems (Bohl 1989). The manner in which the workforce reductions are undertaken has a significant impact on the organisation’s success in managing the survivors.

Literature has stressed a number of employee related outcomes or issues arising out of post mergers. The next section of the literature discusses the same.

2.3.1 (b) Employee Related Issues: There are differences in how various employees view a merger (Costello et al., 1963; Marks,1982). For example, employees who are satisfied with management’s handling of communication issues are usually more positive about a merger. Also, less successful
employees may view a merger as a 'second chance' for success in their careers. Some of the positive outcomes include greater job satisfaction, improved scope and variety of work, increased status, prospects for promotion, compensation, and more job security in a larger firm (Sinetar, 1981).

However in general, these are the common (mostly negative) reactions, typically attributed to employees in the acquired firm. There is widespread anxiety and stress, concern about job security, fear of decline in status or career prospects and feelings of being 'sold out' (Blake and Mouton, 1985; Ivancevich et al., 1987; Marks and Mirvis, 1985; Wishard, 1985).

The survey results by Chambers, K. and Honeycutt, A. (2009) have indicated that following a merger, the low morale of employees had led to reduced organisational commitment. Low morale would have been caused by insecurity about jobs, changes in processes, management, or a new pay structure. Schweiger, Ivancevich and Power (1987) found that 58% of managers in an acquired firm are gone within 5 years or less after an acquisition.

In a study of middle managers involved in the merger of two United Kingdom building societies, the post-merger measures of mental health suggest that the merger was a stressful life event. The two organisations were strategically and culturally well matched and the culture integration was a relatively smooth process; however, the merger was still stressful. In post-merger measurements it was found that the middle managers from both groups had adverse mental health scores significantly higher than the normal population. These findings are consistent with earlier research (Ashford, 1988) in emphasizing that any major organisation change is likely to be stressful.

Employees often cope with the uncertainty surrounding a merger by reducing levels of commitment or try leaving the organisation (Fulmer and Gilkey, 1988). Schweiger and Denisi’s also mentioned that the negative effects of
mergers do not seem to simply diminish with time, but rather seem to get more serious with time. Acquired firm employees, may suffer from feelings of worthlessness, and inferiority because of loss of power. The imbalance of power inherent in the acquirer/acquired relationship has also been shown to affect behavioural outcomes. Studies done by Covin, Sightler, Kolenko and Tudor (1997) revealed that post-merger, employees of the acquired firm had significantly lower satisfaction scores than either employees of the acquiring firm or new hires.

Robino and Demeuse (1985) surveyed personnel managers who had been involved in a corporate merger or acquisition. In a study they measured employee job satisfaction before and after the merger on eight factors. All these eight factors of satisfaction showed a decline in levels for employees of the acquired companies. Likewise, even in the acquiring companies’ managers felt that job satisfaction decreased in most instances, but not to the extent as in the acquired companies.

However studies by Cartwright and Cooper (1993) found no difference in job satisfaction between the acquired and acquiring company employees.

In continuation with the earlier findings it is expected that,

- *Employee satisfaction with HR interventions will depend upon whether they belong to acquired, acquiring or merged entity*
- *There will be a significant positive correlation between HR interventions and Employee satisfaction*

The literature has given different findings on how employees of different organisations react to the merger.
One of the most common reactions in mergers and acquisitions is a sense of loss, both in a general sense and the specific loss of control over one's career, autonomy, and organisational identity. Post mergers, negative reactions may lead to lower job satisfaction (Buono and Bowditch 1989) an increase in unproductive work time and greater turnover and absenteeism (Cabrera, 1982, Robino and Demeuse, 1985).

The study done by Lipponen (2004) investigated the effects of procedural justice perceptions on employee responses to an organisational merger. Procedural justice turned out to be a strong predictor for both post-merger organisational identification and the common in group identity. The degree of identification and perceptions of the common in group identity had increased post mergers as the employees perceived that the implementation process during the merger was fair.

In a research done by Teresa (1997) post-merger satisfaction levels across pay class (e.g. senior managerial versus junior employees) were quite different. It was found that the junior level employees are more satisfied in comparison with the middle and top level managers.

The study done by Dimitris (1997) found that employees in senior hierarchical positions are more likely to be affected by the acquisitions, as they have the power to influence certain decisions. It was also seen that for/among these employees the turnover was much higher as compared to line or lower level managers.

Mergers and acquisitions represent change, and it is this change that generates different emotions among different employee groups. While employees from an acquiring company may feel excited about the new challenges that the integration brings to them, employees from an acquired company may have very different reactions, such as feeling anxious, uncertain, or even intimidated as they go through major changes (Machiraju, 2003). In the face of
organisational changes from M&As, employees tend to be worried with issues such as job security and their future careers with the organisation (Daniel & Metcalf, 2001).

The research paper by Dimitris (1997) further argues that when the expectations for post-acquisition performance are not met, the managing teams of both companies and the employees of the acquired company enter a “cycle of escalating conflict and distrust”. Managers of the acquiring company press for increased control, while employees of the acquired company resist and demand their autonomy.

Research by Applebaum (2007) has explained how leadership style throughout the merger process can significantly affect its outcome. It is proven that leadership style influences employees’ post-merger satisfaction. Furthermore, employees need clear direction so to avoid misunderstanding. Managers can affect the final result of success or failure of a merger through the selection of change management strategies. The HR can play an important role in managing the change process.

A Study by Bhatnagar.J (2007) on 640 Indian managers from 50 Indian organisations showed that there is a positive correlation between strategic HR roles and improvement of organisational commitment in the organisation. HR plays an important role in increasing the commitment of employees post mergers.

Astrachan (1990) explores the psychological, emotional and behavioural impact of mergers and acquisitions in a systematic analysis using the concept of separation anxiety in his book, “Mergers, Acquisitions and Employee Anxiety”. He tests separation anxiety theory using a merger and acquisition simulation. Separation anxiety is a narrow facet of the whole change process which, according to Astrachan’s research, has extensive effects on individuals and groups. The results of his research indicate that the effects of separation
anxiety are influenced by the number of people separating. It produced stress because individuals increased the strength of their attachments without preparing for separation; therefore, making separation more emotionally stressful. Also, prior separation experiences greatly influenced later responses to separation anxiety. The results also suggest that separation anxiety can be managed; reducing negative effects while emphasising positive aspects.

Given the magnitude and importance of the employees’ psychological reactions on the outcome of the merger, it is very important to understand the sources of this stress and the way it affects the organisation. Literature has identified six theories regarding what causes stress and how to deal with it/suggested interventions.

a) **Anxiety Theory**: Mergers and acquisitions cause anxiety due to uncertainty. Employee productivity reduces as they may get anxious about the future outcomes. (Buono& Bowditch, 1989) This can be reduced if leaders can address the employees about what is going to happen to the organisation and to their jobs during the communication process. It is also suggested that organisations provide accurate information at regular intervals through a formal channel.

b) **Social Identity Theory**: Those employees who strongly identify themselves with their previous organisations are more likely to feel a strong sense of loss, anger, and grief when facing M&A and therefore are less likely to accept the change initiatives post M&A. (Ashforth&Mael, 1989; Kramer, 1991) People are also likely to develop strong in-group/out-group biases, which can lead to serious inter-organisational conflicts. HR should ensure and meet these employees of the acquired organisation on a one to one basis.

c) **Acculturation Theory**: M&A also involves combining two distinctive organisational cultures or imposing one over the other. Therefore, it is likely for employees, especially from the acquired firm, to experience significant stress
and tension while adjusting to a new organisational culture. It predicts that when organisational members’ desire to maintain their separate culture is strong, the acculturation tensions and conflicts will be the highest. In order to reduce stress and conflicts arising out of acculturation it is suggested that companies facilitate intercultural learning. Intercultural presentations and workshops have been considered as a useful intervention. (Cartwright & Cooper, 1993).

d) Role Conflict Theory: Role conflict theory suggests that role ambiguity and conflict is another source of stress, which may lead to lower work motivation and higher job dissatisfaction. Researchers believe that to deal with this problem two-way communication should be encouraged in organisations, which consists of both- active listening and promptly responding to the role-related issues. Designing a formal transition structure (or parallel organisational structure), such as a steering committee and various task forces, has been also recommended as an effective intervention. (Mark & Mirvis, 1992)

e) Job Characteristics Theory: M&A brings changes in career paths, work relationships, status differences, geographic transfer, and job security (Newman & Krzystofia, 1993). According to the job characteristics theory, employees’ attitudes and behaviour changes depending on how favourably or unfavourably they perceive changes in the actual job-related elements post-merger. Employees’ attitudes and behaviour could be changed for the better if they expect and/or experience a better job environment after a merger. A related managerial practice is carefully redesigning jobs in the post-M&A organisation in a way that employee’s job satisfaction should sustain or increase.

f) Organisational Justice Theory: Organisational justice theory predicts that employees may pay close attention to how certain important decisions are made and how people are treated with regards to both procedural and distributive unfairness during the M&A (Greenberg, 1987). More importantly, it suggests that their perceived unfairness in the processes and outcomes of those decisions
may negatively affect their satisfaction, commitment, and trust, and intention to stay after a merger. Allowing equal participation of employees from both organisations in making important decisions, developing new human resource management procedures in the newly merged organisations can reduce the perceptions of unfairness substantially.

Thus different theories of stress have highlighted the ‘stress’ levels post mergers and ways of handling the same.

Covin et al. (1997) uses the attitudinal and demographical variables as predictor variables for merger satisfaction. Although little information regarding demographic influences on individual merger satisfaction is available, one would intuitively expect that particular personal characteristics might predispose an individual toward favourable or unfavourable merger attitudes.

Analysis by Davy et al. (1988) involves a field study at 2 separate stages: the first less than a month after the completion of the sale and the second one three months later. The objective was to judge the impact on employee’s attitudes, performance and behavioural intentions over time. Their findings show that employee’s attitudes and intentions to leave and absenteeism deteriorated between the first and the second survey. The feelings of job insecurity significantly increased, which is consistent with the fact that layoffs indeed did occur during the three-month period between the surveys. Also, organisational commitment significantly decreased, while intentions to leave and absenteeism increased.

2.3.1 (c) Managing cultural integration: According to Miller (2000) mismatch of two corporate cultures can be a key factor in the failure of a merger or acquisition. Cultural differences at the top management level are most likely to influence the merging organisations’ ability to realize synergies.
Shelton, Hall & Darling (2003) in their research paper, have studied the case of Daimler Chrysler merger. The case is a classic example where the failure post merger was attributed to the cultural mismatch of both the organisations.

According to Harshbarger (1987) organisational culture is part of the employee’s identity. According to Marks and Mirvis (1986) the most important source of conflict in an acquisition is the clash of cultures that occurs when the dominant firm attempts to subvert the formal and informal organisation of the acquired firm.

Buono, Bowditch and Lewis (1988) have added to the research by studying a merger between two mutual savings banks from the perspective of organisational culture. They compared each bank’s culture and organisational climate before the merger with the resultant culture, and climate surveys after the merger. The results of the study indicate that there are major difficulties in merging two different organisational cultures. The implications of this research to those involved in mergers and acquisitions are to consider the organisational culture carefully of each organisation when embarking on a merger or acquisition.

Though research suggests that pre-merger cultural audit is a critical factor for the merging entities, study done by Lodorfos and Boateng (2006) found that managers pay less attention on the target selection criteria, and do not analyse thoroughly the cultural fit of the merging entities especially during the pre-merger stages.

Nahavandi and Malekzadeh’s paper (1988) has formalized the role of socio cultural factors in the merger process. Their model is an adaptation of theories from cross-cultural psychology and tries to explain the process of cultural adaptation and acculturation in mergers. They identify four modes through which acculturation takes place: Integration, Assimilation, Separation and
Deculturation. In their model, characteristics of merging firms will determine which mode of acculturation will be triggered.

Elsass and Veiga (1994) follow the anthropological framework proposed by Nahavandi and Malekzadeh, but they opine that acculturation is affected by inter-group dynamics that encourage groups to maintain separate and unique cultural identities, and organisational requirements for interaction and organisational integration. Under this model, there are four initial outcomes: Deculturation, Separation, Assimilation and Acculturative Tension. They argue that an increase in performance will reinforce the initial outcome and that a reduction in performance will tend to modify cultural forces, integrate cultural forces or both. Thus, they propose that performance has a feedback effect that helps to reach a stationary state or, the so called, final acculturation mode.

Buono and Bowditch (1989) suggest that there are two fundamental ways of introducing cultural changes in an organisation after a merger. a) The first is getting employees to accept a new set of beliefs and values by studying their attitudes and then trying to change their associated behaviour. b) The second way to induce cultural change is to recruit and socialize new members who fit into the culture while removing those who do not fit. It is possible that many of the deviants may voluntarily leave the organisation.

On the other hand, Shrivastava (1986) suggests that cultural integration should be phased over time to avoid the shocks associated with changes in ownership. According to Schweiger and Goulet (2005) in a merger or acquisition, cultural differences are likely to give rise to ego defences that encourage maintaining individual identities of the acquirer and target. The elimination of cultural differences is therefore an important step towards successful integration.
It is therefore very important for HR and senior management team to avoid the ‘we/they’ attitude by carefully and strategically mixing employees as much as possible at all organisational levels.

2.3.1 (d) Harmonizing HR policies and processes: Although there has been little research in this area yet, in a merger where a major change in human resource policies is probable, i.e. redesign and collaborative mergers, the areas likely to change first are compensation and benefits policies (Steele and Osborne, 1983). Such areas are likely to change first because they are tangible, affect all employees (as opposed to certain groups like executives), and are more technical in nature, allowing specialists to examine them and make recommendations. As these policies are more visible, they are likely to lead to cross-firm comparison among employees, further undertaking the need for consistency of policies (Marks, 1982).

To harmonize these compensation structures effectively, it is imperative for HR to thoroughly understand the disparities in the pre-merger compensation structures of the two firms and develop appropriate compensation packages. Therefore it becomes critical for HR to look into the old benefits of employees to design new compensation structure according to Gaver and Gaver (1993).

In general, the literature is inconsistent on the timing of changes in human resource policy. Searby (1969) suggests changes should be immediate, upon consummation of the merger. Barrett (1973) argues for a phased approach, with the first three to six months used to retire or replace managers whose skills are no longer compatible with the merged firm’s goals and the second 3-6 months used to adjust human resource policies.

Zinghem and Schuster (2001) suggest that a wide range of alternatives exist for making rewards work in favour of both the companies and their workforce. These include implementing total reward solution of dominant, realignment of
the reward practice of the acquired company with that of the acquiring company, retaining acquired company’s pre-acquisition reward practice- here acquirer allows the acquired company to maintain its pay and reward practices as they existed prior to the merger, particularly if the organisations are in different industries and in different stages of maturity or designing a totally new reward solution.

Sharing operational know-how is often important issue post integration. The key word is sharing. Knowledge usually flows from the acquirer to the acquired. The knowledge management literature has mentioned the potential of acquisitions as a means of gaining access to new knowledge. (Madhok 1997); has stressed the importance of knowledge transfer for the acquisitions to create value.

**Handling Unions**

The study of union mergers is typically conducted from industrial relations perspective; with the vast majority of merger studies typically holding to a sociological level of analysis. Waddington (2000) outlined the structure of union merger literature in terms of the union merger process. This process is described according to two dimensions, the first relating to the impact of mergers on the overall development of union structure, and the second describing a process whereby the completion of one single merger is reached. Within the first dimension, researchers are primarily interested in merger frequencies and merger waves, and how these are associated with developments in the number of unions and their sizes. The basic assumption is that, through merger, unions become fewer and larger, as they attempt to increase bargaining power and representation efficiency. The second dimension outlined by Waddington (2000) concerns the process of internal merger negotiations, which subdivides into three inter-related stages: motives for merger, choice of specific merger partner, and specific merger outcomes.
Both forms of participation, however, require that a dialogue take place between the leaders and rank-and-file in which both sides are adequately informed and committed to listening to each other. Consequently, union delegates play a major role in ensuring that transparency characterizes the merger negotiation process leading up to a final decision. In order for a membership to be participative in union activities, their leadership must be responsive and attentive to their members’ willingness to participate.

Strauss (1991) proposed that in order for union democracy to exist at the local level, there has to be a core of committed members who perform the following three functions:

1. Scrutinize union leaders’ power.
2. Provide a nucleus of electoral opposition when needed.
3. Act as a communications link between the leadership and the rank-and-file.

The role of HR thus becomes critical to negotiate with the union members and find out the best possible solution for the workers and the team.

2.3.1 (e) Communication: Another element of the process, which is important in determining how employees react to the acquisition, is the way communication with employees are handled. The literature on the quantity and quality of information that employees must possess (Schweiger and Walsh, 1990), as well as on the timing of communication (Eisenberg and Witten, 1987) is controversial. Most researchers tend to agree that communication with employees during the process is essential for the smooth functioning of the company.

Marks (1982) supports the view that communication creates a climate of security and certainty whereas lack of communication creates a climate of
uncertainty and stress. Lack of communication increases rumours. Marks and Mirvis (1986) mention that when the quality and quantity of communication are low, rumors increase to fill informational gaps, productivity decreases, while turnover increases.

Role of HR in sending the management message and using the right medium of communication to the audience becomes important.

Schweiger and DeNisi (1991), in their study suggest that realistic communication during a merger process in the form of a realistic merger preview can reduce uncertainty and absenteeism amongst the employees. The study done by Julian Birkinshaw (2000) established a high positive correlation between effective communication strategy and post-merger employee satisfaction.

Galpin and Herndon (2000) emphasize that effective communication during a merger should be linked to the strategic objectives of the integration effort. Communication should be honest, proactive and should be planned with ample lead-time and disseminated early.

Papadakis (2005) found that increased communication frequency to the employees after a merger or acquisition leads to increased success in the implementation process.

Davy et al (1988) designed a study to determine the impact of management communication on employee’s attitudes, intentions to leave, absenteeism and performance. Post-merger and acquisition it was found that a good communication programme has positive employee attitude, less absenteeism, better performance and increases the chances that the employee will stay back. Literature has put in place the different issues arising out of post mergers and acquisitions. It has also highlighted the impact mergers have on employees.
The next section will discuss the interventions used by HR professionals to handle these issues.

2.3.2 HR interventions in Mergers and Acquisitions

Despite late involvement of HR function in the merger process, researchers have recognized the important role it plays in integrating people. Various interventions have been suggested to facilitate the process of HR integration. The term intervention refers to a set of sequenced, planned actions or events intended to help an organisation to increase its effectiveness. Interventions purposely disrupt the status quo; they are deliberate attempts to change the state of an organisation or sub-unit toward a different and more effective one (Beehr & O’Hara, 1987). The focus of the interventions can be on the structural, technological, people, physical or cultural setting areas (Robbins, 1997):

- Structural interventions may involve change in organisational design, decentralization and modifying the flow of work;
- Technological interventions may involve interventions such as job enrichment and job enlargement;
- People interventions involve interventions to improve organisational performance causing the employees to become more productive. Such efforts are known as organisational development (OD) techniques, behaviour modification and management by objectives;
- Physical setting interventions include the layout of the workspace, interior design and equipment placement;
- Organisational culture interventions refer to changing shared symbols, rituals and beliefs. Change in this area is usually difficult and managers are advised to proceed with caution.
The merger and acquisition intervention describes how HR can assist two or more organisations to form a new entity. These interventions move the organisation beyond solving existing problems so as to become capable of continuous improvement.

In a paper written by Christine (1995) the authors discusses the merger between Lloyds and Midland banks with HSBC Holdings and the interventions used by the HR professionals. An ongoing programme of career development interviews was been carried out by the HR function with the support of line management so as to balance the individual aspirations with business needs of the new entity. The HR also carried out an assessment of each job post-merger. This was done to provide a correlation between the two existing grading systems. The new grading system was explained to each and every employee and all questions were answered.

In a paper written by Jane (2003) an example of The New Zealand based banking merger of Westpac and Trust Bank the author considered communication as an intervention tool used by the HR professional. The communication strategies, selection processes, alignment of HR policies, and training and preparedness strategies, were all important in contributing to staff experience of the merger. The communications project team with HR devised strategies to keep staff well informed via regular newsletters, faxes, videos, booklets, presentations and meetings. Much of the communication was led by the Chief Executive Officer and HR in an effort to reinforce the driving communication value of “as soon as we know, you’ll know”. The strategies facilitated feedback. The selection processes differed according to the level of the positions, but examination of the selection processes shows that all aimed for consistency. Significant work was put into the alignment of HR policies and practices in the banks. A range of training and preparedness strategies were developed. This developed trust factor in the employees post-merger.
In a paper written by John, Philip and David (1998) the authors discuss how, mentoring was an important intervention for learning and coping with organisational change post-merger in two international accounting companies. The HR appointed some senior executives as mentors in the merged company. The roles of these mentors were to answer the queries of the mentees post mergers. The mentors were constantly in touch with their mentees and answering some common questions like:- How has the new job to be done? How will the new evaluation be done? How to deal with the new clients? The results obtained by HR showed that psycho-social mentoring was an important source of confirmation and self-esteem during the merger.

An empirical study done by David and Yaakov (2002) on 80 companies lists the common interventions used by most of the organisations post-merger. The HR respondents were presented a list of 12 interventions used to help the acquired employees and work teams post mergers and asked to indicate their importance. The various interventions highlighted were:- training managers to deal with employees concerns during organisational and individual changes, stress management training programmes, professional psychological counselling, employee moral surveys, organisational and unit effectiveness assessment, career counselling, skills retraining, team building, conflict resolution programmes, meetings to allow employees to share common concerns, meetings or ceremonies to mourn the loss of acquired firms and merger sensitation workshops.

In a research done by Schweiger and DeNisi (1991) employees were given a “realistic merger preview” consisting of a letter from the CEO on how the merger would affect them. They also had access to a merger hotline, and weekly meetings with the HR and the plant manager was done. Managers provided employees with frequent, honest and relevant information about the merger, handled employees fairly and answered any questions and concerns the employees might have, to the fullest extent possible.
Research by Kevin D. Wilde (2003) found that when General Mills acquired larger rival Pillsbury in 2001, it structured its transition strategy around key HR systems and methodologies that it believed would build strong employee commitment to the new organisation and a shared culture for success. Two years later, all signs indicated the strategy was a winner. The company had realized the cost synergies and productivity gains envisioned in the acquisition. The perceptions of the workforce indicated a culture, a performance orientation, and a level of commitment in line with the objectives of the new organisation. The company was able to retain 98 percent of the “top value creators”. Retention rate had increased. The commitment levels and satisfaction of all the employees was high. These were due to the HR interventions used in the organisations.

Larsson and Lubatkin (2001) have suggested a list of interventions which can be adopted by HR to eliminate the cultural differences in both the organisations. Activities like introduction programmes, visits to each other’s sites, celebrations, and socialisation rituals could bridge the gap between both the organisations. This process of learning and developing empathy can be accomplished if one discovers the limitations of one’s own culture and the positives in other cultures. The elimination of cultural differences is therefore an important step towards successful integration which should be done by the HR post merger.

In continuation with the earlier findings it is expected that,

*The effect of HR interventions on employee satisfaction is dependent on the hierarchical level of the employee in the organisation.*
2.4 Best Practices in Mergers and Acquisitions- Models of Integration

Given the complexities of integrating target companies, wide variations in characteristics from one deal to another, and high failure rate of existing deals, the question that has to be answered is how can HR maximize their chances of success post mergers? Recent literature has pointed to several “best practices”. The literature below highlights some of the models used by organisations.

2.4.1 Pathfinder Model

Over the years, GE Capital Services' acquisition-integration process has been discussed, debated, tested, changed and refined. Ashkenas, DeMonaco and Francis (1998) in their paper ‘Making the Deal Real: How GE Capital Integrates Acquisitions’ have discussed the GE model which is commonly called the Path finder model.

The model divides the process into four "action stages," starting with the work that goes on before the acquisition is completed that is, before the deal closes, and continuing all the way through assimilation. There are two or three sub processes in each action stage, such as due diligence during the preacquisition stage and strategy formulation during the foundation-building stage. Finally, each action stage includes several best practices – specific and practical steps managers can take to support the process. The model's neat and systematic appearance underlines the fact that acquisition integration is as much an art as a science.
The Pathfinder Model recommends a particular sequence of leveraged actions, but there are aspects of each acquisition-integration process that are new or unique. Each stage includes best practices and practical steps to be taken by managers. Acquisition integration begins with due-diligence. Integration management includes recognizing different functions like finance, operations etc. A successful integration includes implementation of management decisions like reporting structures, layoffs etc., i.e. technical aspects and also
the cultural aspects. Rapid integration phase also includes designing process maps to accelerate the integration as well as audits and feedbacks if required.

2.4.2 FIDESS model

J. Vester (2002) designed an integration process model called FIDESS model after studying the acquisition of Xerox and Tektronix’s Printer Division in the year 1999.

FIDESS stands for Focus, Innovation, Discipline, Excellence, Speed and Simplicity. The program contained six phases beginning at the completion of due-diligence. The six phases include pre-announcement, joint integration planning, first day execution, integration, 100-day assessment and correction, and on-going integration.

In each of the phases he has discussed the specific goals that the organisation needs to set with respect to the senior management which becomes an important part of the model. Vester has also kept the model flexible for the unseen and unavoidable situations that may surface during the post-acquisition integration.
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- Make senior executive visits
- Move people into the same locations
- Keep the target’s management team together

- Jump start the project as early as possible
- Make decisions quickly
- Appoint and announce new management quickly

- Bring in outside experts
- Acquire excellent companies
- Utilize the new talent
- Be patient with progress
- Appoint full-time integration team leaders & members
- Go for ‘A’ players
- Reward successes regularly

- Plan, re-plan and plan again
- Build in regular, formal reviews
- Manage synergy capture
- Develop robust communications

- Organize integration for functions and geographies
- Share best practices on the integration team
- Protect the acquired organisation
- Make a decision ‘log’
- Address existing management processes dispassionately

- Ensure a solid strategic rationale exists for the acquisition
- Lay out the expected financials in advance
- Develop a realistic integration timeline
- Ensure ‘line’ ownership for the acquisition’s success

Fig. 7 FIDESS model
2.4.3 Human Capital Model

Nalbantian et al. (2005) proposed an integration model called the ‘Human Capital Model’ focusing on the degree and speed of integration. Just as Pablo (1994) in his paper has discussed the three levels of integration, the core of the Human capital model contained three degrees of integration: (a) complete assimilation of the acquired company, (b) partial absorption of the acquired company, or (c) a portfolio arrangement referring to little or no integration of the acquired company such as a wholly-owned subsidiary, the model has two elements, the barriers and the forces, which take place during integration.

Barriers included factors like demographics, cultural dissimilarities, degree of autonomy, employee selection and training processes, compensation incompatibilities etc. Forces include strategic intent, human capital requirements, core business process requirements, or a combination of the three.

Barrier and force dimensions when mapped into a two-by-two matrix with four cells provide different combinations of integration process.

The barriers high and forces low cell resulted in a portfolio type of integration. The barriers low and forces high cell demanded a full and rapid integration approach. In the cell with integration barriers and forces rated low, the outcome ranged from a portfolio to a partial integration approach. In the cell with integration barriers and forces rated high, the combination required a full but slow integration approach. The model provides a valuable insight on integration approaches from a human capital point of view.
2.4.4 Merger Management model


The two pillars of the model are disparity and goodwill. Disparity is the degree of similarity between combining companies and goodwill is the excess amount above book value paid for a company and represented the expected added value of a merger or an acquisition. Crossing these two dimensions formed four acquisition type quadrants at the core of the M3. The combination of goodwill and disparity provides different degree of integration required.
The upper left quadrant reflected high goodwill and low disparity, focused on synergy during integration, and required a slower integration timeframe with succession planning. The upper right quadrant reflected high goodwill and disparity, focused on continued performance and preserving value during integration, and required a lower degree of integration. The lower right quadrant reflected low goodwill and high disparity, highlighted potentially problematic combinations, and required a vertical or portfolio approach to integration. The lower left quadrant reflected low goodwill and disparity, focused on reducing costs and growing market share during integration, and required rapid comprehensive integration approach.

The literature on post-merger integration gave a lot of insights on what are the HR challenges to be handled post mergers. Though the different models on integration had a lot of similarities; there was no specific model or answer on how horizontal post-merger and acquisition integration has to be handled.

According to Seo and Hill (2005), each type of merger and acquisitions is unique as it involves different degree of integration. Selecting one approach or model is difficult as there are different variables to be applied in each. The study is not benchmarking any models, however as mentioned, one of its objective is to provide a road map or checklist for the HR professionals who would be handling a merger or an acquisition in the future.