

THE PHENOMENON OF MERGER AND ACQUISITION WITHIN THE AUTOMOTIVE INDUSTRY

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ABSTRACT

M&A is a way to survive and succeed in a competitive global environment as a consequence of new political, monetary and regulatory issues. The complex phenomenon that M&As represent has received consistent attention from the research community over the last 30 years. Large scaled M&As between automotive manufacturers, like the Daimler-Chrysler merger, the alliance between Renault and Nissan and the acquisition of Volvo by Ford, have attracted significant attention in the last decades. However, apart from this considerable interest, the findings on the general performance of automotive M&As are inconsistent and contradictory. This paper is focused on some critical success factors in automotive M&As like the connection between pre-acquisition and post-acquisition processes, turnover of key people etc. The phenomenon of merger and acquisition within the automotive industry needs further research and discussions due to the fact that some strategic alliances and M&A proved to be successful (e.g. Skoda - Volkswagen) and others not (e.g. Rover - BMW).

KEY WORDS: *mergers and acquisitions (M&As), M&A performance, automotive industry*

JEL CLASSIFICATION: *G34, L62, Z19*

1. INTRODUCTION

Global business expansion through mergers and acquisitions is one of the most important forms of growth in the last decades. M&A is a way to survive and succeed in a competitive global environment as a consequence of new political, monetary and regulatory issues. M&A is a multilevel, multidisciplinary, and multistage process which involves, usually, organizational change, integrating some or all parts of the original organizations' functions, processes and activities.

Mergers and acquisitions (M&As) continue to be very popular but also controversial due to the high failure rate. This suggests that neither scholars nor practitioners have a clear understanding of the factors involved in the M&A process and their complex interrelationships. M&A success, a disputed subject, is a combination of strategic and financial complementarity, degree of integration and cultural fit.

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As one of the world's largest manufacturing industries, the automotive industry has the capability to influence the labor, trade and capital markets and also governments' macroeconomic and industrial aims. Contrary to notorious myth, the automotive industry is not shrinking due to economic crisis.

Large scaled M&As between automotive manufacturers, like the Daimler-Chrysler merger, the alliance between Renault and Nissan and the acquisition of Volvo by Ford, have attracted significant attention in the last decades.

The main motivations in automotive M&As are:

- economies of scale
- geographic market expansion
- risk reduction and diversification
- leveraging of core competencies and technological changes

The automotive industry has faced with consolidation already in the early phases of its rise in the beginning of the 20th century, by the acquisitions of Vauxhall (United Kingdom) and Opel (Germany) by GM (United States) in 1925 and 1929, respectively. In the last decades, numerous M&As have been accomplished: the acquisitions of Chrysler (United States) in 1998 and Mitsubishi (Japan) in 2000, by Daimler-Benz (Germany), the acquisition of Jaguar (United Kingdom) in 1989, Volvo (Sweden) in 1999 and Land Rover (United Kingdom) in 2000 by Ford (United States) and the takeover of Seat (Spain) in 1986 and Skoda (Czechoslovakia) in 1990, by Volkswagen (Germany).

Notwithstanding, the consolidation in the automotive industry has not always been successful. Two popular examples of failures include acquisition of Rover (United Kingdom) by BMW (Germany), ending in 2000, and the divestment of Chrysler by Daimler-Benz in 2007. Still, this market has also seen successful examples: the alliance between Renault and Nissan and the acquisition of Skoda and Seat by Volkswagen.

2. WHAT IS THE LOGIC OF M&AS?

Given the rapidly shifting corporate and global landscapes, if we are to keep pace with the speed of change, learning and innovation occurring in the companies that we study, we need to be ready to maneuver ourselves as researchers engaged in studying one of the most prevalent forms of change in modern corporate history: M&A, as Cartwright et al. (2012) point out.

In a recent study, DePamphilis (2011) stated that the first decade of the new millennium heralded an era of global megamergers. Like the mergers and acquisitions (M&As) frenzy of the 1980s and 1990s, several factors fueled activity through mid-2007: readily available credit, historically low interest rates, rising equity markets, technological change, global competition, and industry consolidation. In terms of dollar volume, M&A transactions reached a record level worldwide in 2007.

The same point of view is offered by Trompenaars and Asser (2010) who observe that global business expansion and development through mergers, acquisitions and strategic alliances is big business. Even in the wake of the financial crisis of 2008/2009, in a climate of banking difficulties and credit restrictions, more and more “share for share” deals are being proposed and effected.

Economic structure, liberalisation and preferential policies, and cultural and legal environment played an important role for attracting FDI as Sahoo et. al. (2014) conclude. The authors point out that in economic structure, market size, and abundant supply of cheap labour, infrastructure, and scale effect are the major determinants of FDI.

DePamphilis (2011) observes that businesses come and go in a continuing churn, perhaps best illustrated by the ever-changing composition of the so-called Fortune 500—the 500 largest U.S. corporations. Only 70 of the firms on the original 1955 list of 500 are on today’s list, and some 2,000 firms have appeared on the list at one time or another. Most have dropped off the list either through merger, acquisition, bankruptcy, downsizing, or some other form of corporate

restructuring. The author considers a few examples: Chrysler, Bethlehem Steel, Scott Paper, Zenith, Rubbermaid, Warner Lambert.

Trompenaars and Asser (2010) point out that business is increasingly pursuing mergers, acquisitions and strategic alliances, not only to implement globalization strategies and necessary restructuring, but as a consequence of political, monetary and regulatory convergence. The authors consider that a few global companies like P&G, J&J, IBM, GE, Pfizer and Cisco but also Tata & Sons, Mahindra & Mahindra, Haier, Lenovo, HSBC, and others all have an M&A strategy coupled with an organic growth strategy, enhancing growth and managing risk at the same time. The conclusion reached by the authors is that realizing the business benefits and creating wealth in an integration process is not a straightforward procedure. Although success rates of mergers and acquisitions are difficult to compare, as surveys in the area use a variety of assessment metrics, most point to a success rate of about one third, while some have found that only 20% of mergers and acquisitions are ultimately successful.

In their study, Very et al. (2012) observe that accurate practical predictions of M&A activity can be made at country level and that the dependence/contagion framework appears appropriate for selecting the possible determinants of M&A activity per country.

Almor et al. (2014) argue that despite their relatively young age, small size, and scarcity of resources and capabilities compared to large technology-based multinational enterprises, born-global companies must use mergers and acquisitions (M&As) to survive and succeed in a competitive global environment.

M&A necessarily involves organizational change, integrating some or all parts of the original organizations' functions and activities (Seo & Hill 2005). The degree of organizational change can vary substantially across M&As because the motives and types of M&As differ widely.

M&A is a multilevel, multidisciplinary, and multistage process which requires a pluralist approach, as Warter and Warter (2014) argue. M&A researchers have focused generically separately on pre-acquisition factors and post-acquisition influential factors. Neither scholars nor practitioners have a comprehensive understanding of the factors involved in the M&A process and their interrelationships.

The findings show that global and host-region firms benefit from cross-border M&As, whereas home-region firms gain value from product diversification but only up to an inflection point, where further product diversification becomes unmanageable as Kling et al. (2014) point out. The authors conclude that finally, the findings illustrate that there is no value-enhancing M&A strategy for home-region and bi-regional firms to become global firms; the phenomenon of regionalization is here to stay.

It can therefore be concluded that M&As are clearly the most important forms of change in the modern economic world, a complex area who requires an interdisciplinary approach.

3. M&A PERFORMANCE - SUCCESS OR FAILURE?

A recent paper (Gomes et al., 2013) claims that merely investigating additional discrete variables, within discipline, may not be sufficient to progress M&A research as this is to fall into a "specialization trap". M&A is a multilevel, multidisciplinary, and multistage phenomenon. It requires a more pluralist approach, with integrative frameworks, to grasp the complexities of this multifaceted, multitemporal phenomenon. Historically, M&A researchers have focused separately on preacquisition factors and postacquisition factors influencing performance. However, failure to find a consistent relationship between synergy potentials of strategic fit and M&A performance has led researchers to recognize that "organizational fit" between companies post deal may be the main determinant of overall M&A performance.

DePamphilis (2011) focuses on the answer to whether M&As pay off seems to depend on whom and over what period. On average, total shareholder gains around the announcement date of an acquisition or merger are significantly positive; however, most of the gain accrues to target firm shareholders. Moreover, in the three to five years after a takeover, many acquirer firms either underperform compared with their industry peers or destroy shareholder value. The author concludes that it is less clear whether this sub-par performance and value destruction is due to the acquisition or to other factors.

Meglio (2009) remarks that although the realm of technology-driven M&As play a prominent role in changing the landscape of several industries, M&A performance in low-tech and service industries deserves further attention. As for the time span, it should be enlarged, from 1970s to date, to account for trends over a longer period of time.

M&A performance is primarily affected by specific M&A characteristics, but not by general market characteristics such as demand development or competition conditions, as Arvanitis and Stucki (2014) remark. The authors consider that rather astonishingly, it is also not affected by firm characteristics such as capital intensity, human capital endowment and firm size.

When a proposed merger falls apart, though, it is likely that the price of the stock of the company being acquired will fall, and in some cases the fall can be quite dramatic as Travers (2004) concludes.

As Chatterjee (2009) observes, when firms first consider an acquisition programme, a common theme among the successful programmes is a clear strategic analysis of the market they are considering.

Marks and Mirvis (2011) highlight that the Merger Syndrome is a fusion of uncertainty and the likelihood of change, both favorable and unfavorable, that produces stress and ultimately affects perceptions and judgments, interpersonal relationships, and the dynamics of the combination itself. At the organizational level, the Syndrome is manifested by increased centralization and lessened communication, leaving people in the dark about the combination and fueling rumors and insecurities. This often produces worst-case-scenario thinking that distracts employees from regular duties. All of this hampers integration, reduces productivity, and contributes to turnover of key people.

In their study, Bauer and Matzler (2014) conclude that M&A success is a function of strategic complementarity, cultural fit, and the degree of integration. The authors argue that strategic complementarity also positively influences cultural fit and the degree of integration. Cultural fit positively influences M&A success, but surprisingly has a negative impact on the speed and degree of integration. The degree of integration is positively related to speed of integration.

In a recent article, Gomes et al. (2013) generally agree with the previous author and notice that the high failure rate of mergers and acquisitions suggests that neither scholars nor practitioners have a thorough understanding of the variables involved in the M&A process and their complex interrelationships. The existing body of knowledge is characterized by several independent streams of management research that have studied discrete variables in either the preacquisition or postacquisition stage. The authors' discussion has highlighted how the value of each of the critical success factors can be enhanced through consideration of how they may relate and be informed by other critical success variables both within and across phases of the M&A process. Their conclusion was that in this way, an interdisciplinary approach to M&A is outlined and a more holistic perception of the phenomena is achieved.

An interesting paper (Meglio, 2010) remarks that findings present a fragmented state of affairs with a proliferation of operational definitions of post-acquisition performance and a wide array of indicators. Moreover, different perspectives and time lags are accounted for. This is a partial explanation for inconsistent and contradictory findings about M&A performance. This analysis can be extended and improved in several ways. A first option is to enlarge the scope and the

time span of the review. Although the realm of technology-driven M&As play a prominent role in changing the landscape of several industries, M&A performance in low-tech and service industries deserves further attention. As for the time span, it should be enlarged, from 1970s to date, to account for trends over a longer period of time. The author conclusion is that findings provide evidence that a serious reflection on construct measurement is needed.

To summarize, M&A success depends on mechanisms that enhance the exploration and exploitation of knowledge as Reus (2012) concludes. Exploration depends on the capacity to absorb new knowledge, which is a function of the amount of prior related experiences of the acquirer and target, and complementary knowledge among acquisition partners. Exploitation of knowledge depends on combinative capability, which is a function of the extent to which acquisition partners have the opportunity, motivation, and ability to share knowledge.

A merger is a dramatic event for companies and employees, for it requires integration of two organizations. Mergers and acquisitions (M&As) have inevitably drawn the attention of many groups of scholars, each of whom studies the subject from a unique perspective. Most surveys on M&A point to a success rate of about one third.

The M&A reasons, as they emerge from our review, can be described as a result of globalisation, of the need of growth and of achieving synergies. The M&A process can be described as multilevel, multidisciplinary, and multistage phenomenon.

M&A researchers have focused generically separately on pre-acquisition factors and post-acquisition influential factors. Neither scholars nor practitioners have a comprehensive understanding of the factors involved in the M&A process and their influence on merger performance.

4. M&A SPECIFIC FEATURES IN AUTOMOTIVE INDUSTRY

Investor's decision to acquire, sell or to carry out projects in a particular area, region or country is not only due to purely economic, commercial or financial reasoning, as Zait et al. (2014) remark. In such operations, meeting among businessmen, managers and other professionals in the field is, first of all, meeting in specific circumstances, among more or less different cultures. Zait (2013) emphasizes that mixing different solutions as cultural origin offers almost always the chance of obtaining a significant intercultural synergy in business, management, negotiation or marketing, etc.

The automotive industry has been "global" for an appreciable period of time. Historically, cross-border M&As have been closely correlated with overall automotive M&A levels. Companies in the automotive industry initiate cross-border M&As mainly to:

- Access new customers in new markets
- Acquire new production capabilities or technology
- Grow with customers in existing markets and following them into newer ones

Another scholar (He, 2009) highlights that the acquisition process may affect performance, as acquiring companies adopting a 'soft approach' or introducing 'gradual changes' are more likely to gain knowledge of the subsidiary progressively. As a result, they may have more time and resources to deal with the challenges and difficulties of the integration process.

When demand in the automotive industry is increasing, the companies' goal is to improve their products by conducting M&A. As demand slows the reason for acquiring new companies switches away from high technology investments to reducing costs. Depressed company valuations enabled top car manufacturers to include improved integration in their cost reduction strategies along with product line expansion.

Trompenaars and Asser (2010) consider that organizations that are able to reconcile their differences will have created competitive advantage. If they do not, they will end up amongst

the 70% of mergers that fail. Every party should contribute, regardless of whether they are the buyer or the bought, the smaller or the larger.

Other scholars (Ulijn et al., 2010) remark that most studies show that more than half of the strategic alliances and M&A do not prove to be successful. Traditionally, scholars focused on 'hard' factors like financial and strategic factors for explaining the success or failure of these external modes. More recently, however, research into more 'soft' factors such as organizational and human resources- linked subjects have increased in importance.

However, the overall success of most M&As still remains subject to further research and discussions. Some failures, like the divestment of Rover by BMW and Chrysler by Daimler, further amplify the need to assess the motivations and the determinants that influence and may explain the complex process in all stages of M&As.

In a recent paper, Warter and Warter (2014) consider that cultural diversity in organizations can be both an asset and a liability. Whether the losses associated with cultural diversity can be minimized and the gains be realized will depend likewise on the managers' ability to manage the negotiations and due diligence processes in an effective manner.

Even though accounting measures seem to be the preferred choice for many scholars and practitioners, not everybody considers them to be optimal to measure performance. Others prefer to capture the degree of conflict at the organisation level or the degree of synergy realization.

Due to the fact that mergers and acquisitions in the automotive sector occur relatively infrequently and unpredictably, these specific M&As present a tough challenge for the top management: linking and managing the pre- and post-merger stages of the M&A.

Marks and Mirvis (2011) highlight that buying a company encompasses strategizing, scouting, assessing and selecting a partner, deal making, and preparing for the eventual combination. The typical approach involves a "tunnel vision" on the financial aspects of the deal. Buyers concentrate on what a target is worth, what price premium, if any, to pay, and how to structure the transaction. The successful approach, by comparison, also emphasizes finance but adds careful attention to how a combination advances the business strategy of a firm, due diligence on behavioral and culture factors that might complicate the combination, and a clear picture of how the firms will be integrated.

Any M&A activity that involves automotive companies from different countries can create significant barriers to successful integration. These barriers, that need to be overcome, can be: local regulations and industry standards, language and local culture etc.

5. CONCLUSION

The phenomenon of merger and acquisition within the automotive industry needs further research and discussions. Some strategic alliances and M&A proved to be successful, others not.

The existing research is characterized by several independent directions that have studied either the pre-acquisition or post-acquisition stage. The value of each of the critical success factors can be enhanced through consideration of how these factors may relate both within and across phases of the M&A process.

It is less clear whether the value destruction in many automotive M&As is due to the acquisition or to other factors, but acquiring the latest technology and attempting to cut costs will remain the main goals in car manufacturers' acquisition strategies worldwide.

The automotive M&A performance is impacted by some controversial issues: the role of prior merger /acquisition experience, how to assess performance, the role of culture and the connection between pre-acquisition and post-acquisition processes.

Despite the economic challenges, the level of automotive M&A activity will continue targeting innovation and new technologies based on key factors as:

- Reemergence of global economy from economic crisis
- High levels of liquidity in carmakers' accounts
- Strategies to expand market share and gain new customers
- Strategies to develop new products

Other determinants in merger and acquisition within the automotive industry are infrastructure, cultural and legal environment and government's policies.

To sum up, the trends in the automotive M&A market are:

- Reduced number of megadeals
- Emerging market players participate in industry consolidation
- Rising exposure to growth-oriented market trends and creativity

Collectively, these findings suggest that further research on the phenomenon of merger and acquisition within the automotive industry is required.

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