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Review of Major Companies Merger Failures in The First Decade of 21st Century

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Abstract: This paper proposes an explanation as to why some mergers fail, based on the information obtained from different research papers published by different authors worldwide. I propose that failure may result from informational asymmetries arising from the pre-merger period, and problems of cooperation and coordination within recently merged firms. I also believe that a partner may optimally agree to merge and abstain from putting forth any post-merger efforts, counting on the other partner to make necessary efforts. I argue that failure may also stem from cultural differences or political unwillingness within the country in case of cross-border mergers. This paper gives a brief idea of why different major mergers failed even after learning so much from the past mistakes.

Keywords: merger failure, reasons (via case studies).

Introduction

Despite observing consistently strong merger activity around the world, a vast number of these corporations seem to be unsuccessful. Indeed, over the last decade (first decade of the 21st Century), 43% of all merged firms worldwide reported lower profits than comparable non-merged firms and “there were countless examples of failed mergers that were unable to achieve the synergies that motivated the deal” (Gugler et al. 2003). It is not surprising that more than half of merged firms end up being divested and this paper proposes a formal explanation of failure in mergers in various firms. One of the main reasons of merger failure can be attributed to lack of coordination between the firms. Indeed, in the organizational literature poor merger performance has often been connected to post-merger coordination problem. Unlike internal development and growth newly merged firms cannot rely on preexisting mechanisms. Of course, there are other reasons apart from organizational difficulties that may lead to failure.

Mergers may fall because of plain “bad luck” because the realization of the uncertainty falls short of the expectation. Unprofitable mergers may further occur because firms may merge to preempt their partners from merging with rivals (Fridolfsson and Stennek, 2005) or managers may irrationally overestimate the Future performance of merged entity, so called managerial hubris, and due to underestimation of internal conflicts or by not foreseeing problems derived from conflicting organizational cultures. I have tried to provide a formal rationale on why mergers fail as is explained by different authors in their research papers. Uniqueness of this paper is that I have only highlighted the major reasons for failed mergers in big firms in the last decade. The remainder of the paper deals with various short case studies regarding the same.

Case Study 1. Sprint-Nextel merger failure

In 2005, a major communication merger occurred, between Sprint and Nextel Communications. These two companies believed that merging opposite ends of a market’s spectrum-personal cell phone and home services, and business/infrastructure/transportation market from Nextel — would create one big happy communication family (for only $35 billion). But the family did not stay together long. Soon after the merger, Nextel executives and managers left the new company in droves, claiming that the two cultures could not get along. And at the same time, the economy started to take a turn for the worse, and customers (private and business alike) expected more and more from their providers. Competition from AT&T, Verizon, and the iPhone drove down sales, and Sprint/Nextel began lay-offs. Its stocks plummeted, and for all those involved, the merger clearly failed.

Case Study 2. General-Electric and Honeywell case

(Jeremy grant et al. 2005) The merger between the two transatlantic conglomerates failed solely because of European anti-trust authorities. The commission declared that the acquisition of assets of Honeywell by GE would be concentration incompatible with the common market. The author too agrees with the European commission decision. The plausible reason being this merger would have created a concentration, a concentration which strengthened a dominant position as a result of which effective competition would be significantly impeded in the common market. GE went to the court for the same but still could not suffice the significant efficiencies involved in the deal that were overlooked though the evidences presented by commission were far from compelling. It merely can be called "bad luck" which terminated such a fantastic deal.

Case study 3. Daimler-Chrysler Merger

Chrysler-Daimler merger was considered the "merger of equals" as both firms performed well and was expected to benefit from each other's strength and capabilities but the merger didn't work well particularly for Chrysler. The Chrysler division which was performing well began losing money and continued to do so for several years. The major cause of this failure can be attributed to cultural differences between the two organizations. Despite perceived similarities between the negotiating parties in national culture, corporate practice and language. The deal eventually went askew and the ongoing merger failed in 2008. The author very beautifully describes the process of failed merger between Daimler-Chrysler and has analyzed it from a cross cultural management perspective. My conclusion is that historical sentiments, feelings and emotions, if not handled well, can cause fatal damage to cross cultural business ventures.

Case study 4. AOL-Time Warner Merger failure

(Wade and Jared 2010) At the height of the Internet craze, two media merged together to form what was seen as a revolutionary move to fuse the old with the new. In 2001, old-school media giant Time Warner consolidated with American Online (AOL), the Internet and email provider of the people, for a whopping $111 billion. It was considered the combining of the best of both worlds: print and electronic, together at last. But the synergy of these two dynamically different companies never occurred. The dot-com bust and the decline of dial-up Internet access (which AOL refused to give up) spelled disaster for the new company. Since the merger, Time Warner's stock dropped 80 %. In fact, the CEO of Time Warner, Jeff Bewkes, embarrassingly announced that the marriage of AOL and Time Warner was dissolved. The reasons for its failure were many like rapid growth of substitutes like Yahoo! and MSN due to which they had to face tough competition in the market. At the same time there was market growth of Broadband, while AOL had the brand and credibility to capitalize upon growth in this area, it lacked the necessary infrastructure. It had to face many non-operational distractions like widely publicized battles with the shareholders and costly lawsuits with Microsoft over the Netscape internet browser. As a result, management had to divert focus from strategic and management planning leading to overall disaster. Personal conflicts and clear lack of strategy and accountability led to their demerger finally in 2009.

Case study 5. HP-COMPAQ Merger

(Preeta Roy et al, 2004) This case study is based merger of two leading competitors in the global computer industry, Hewlett-Packard Company (HP) and Compaq Computer Corporation (Compaq).The case explores the reasons for HP's failure to realize the synergies identified prior to the merger. On September 04, 2001, two leading players in the global computer industry - Hewlett-Packard Company (HP) and Compaq Computer Corporation (Compaq) - announced their merger. HP was to buy Compaq for US$ 24 billion in stock in the biggest ever deal in the history of the computer industry. Critic called it a strategic blunder and even the dumbest deal of the decade. Together, the pair lost US$ 13 billion in market capitalization in a couple of days. Major reasons for the failure of this deal can be attributed to lack of proper strategy. HP culture was largely based on engineering and compromise, while Compaq had a hard-charging sales culture. Management too in this case was bit autocratic and centralized rather than being free and flexible.

Case study 6. Telia-Telenor Merger

(Meyer and Attenborg 2008) Telenor and Telia the two leading Scandinavian telecomm corporations decided to merge in year 1999. Telia belonged to Norway and Telenor was of Sweden. The Financial times claimed that the merger would be a "Jewel of Communication" and said that this deal marked a new era for the telecommunication sector in Europe. But soon afterwards the situation grew grim and the two companies decided to chuck off the deal. The major cause being incompatible corporate strategy, language and the governance structure which was meant to protect and preserve the national heritage made it very difficult for both the parties to agree on corporate strategies. Conflicts also emerged in the top management. There were also many differences in organizational structure too. At last it can be said that historical sentiments, feelings and emotions, if not handled well, can cause fatal damage to cross-cultural business ventures.

Reasons for Failure

- **Poorly Managed Integration**:

Management plays an important role in the integration of companies, it requires lots of planning. If organization doesn't do that it fails such attempt, poor management results in failure of good deals.

- **Size issue:**

Some time difference in size of companies also creates problems. Many mergers fail either because of 'merger indigestion' through buying too big targets or by not giving the smaller mergers the time and attention it required.

- **Lack of experience** :

Experience plays an important role in any activity, Previous experience will help the acquirers to learn from the previous merger mistakes and help them to make successful mergers in future.

- **Lack of proper Strategic fit**:

If strategic fit between 2 merging companies are good, then merger will yield synergistic gains. Mergers with strategic fit can improve profitability through reduction in overheads, effective utilization of facilities, the ability to raise funds at a lower cost, and deployment of surplus cash for expanding business with higher returns.

- **Cultural Issues**:

The factor which plays an important role in integration is cultural issue. Lots of mergers fail because of cultural difference. Cultural fit and integration of organization are very closely related. It's very difficult to do a successful integration without cultural fit. Some studies examine the effects on post-merger profitability of product and resource relatedness (Singh and Montgomery, 1987; Shelton, 2003). Cultures are typically an integral part of an organization. Cultural is something that that defines the member of that organization; it keeps them together by creating a sense of cohesion. Dismal success rate of merger can be attributed to incompatible cultures. In fact cultural fit is as important as structural fit in analysis and evolution of potential partners. Lack of cultural fit between the merging firms will amount to misunderstanding, confusion and conflict. Therefore, proper cultural due diligence is required for the success of M&As. It is useful to know the target management behaviour with respect to dimensions such as centralized versus decentralized decision making, speed in decision making, and time horizon for decisions, level of team work, and management of conflict, risk orientation and openness to change. The failed merger between TELIA AND TELENOR provides a cogent example of the importance of culture fit. Organization culture is a product of successfully adapting to the environment. Before doing the integration, it is necessary to identify the impact of cultural gap. If cultural issue is not addressed properly, it results in failure of integration which happened in case of HP-Compaq. HP's culture was largely based on engineering and compromise, while Compaq had a hard-charging sales culture. Webet and Camerer (2009) undertake laboratory experiments and prove that failures to coordinate activity based on cultural conflict, contribute to the widespread failure of corporate merger.

- **Failure of Top Management to Follow Up**:

Sometimes top management doesn't make much effort in making things happen. Top management follow up is essential to go with map of action to be taken and also has to set the pace for implementation. Initial few months after the integration decide the pace of growth.

- **Communication**:

Communication plays a vital role in any activity**. Lack** of proper communication in M&A's creates lots of uncertainties. The objective of proper communication is to minimize as much uncertainty as possible, especially with regard to issues that directly impact people and organization. If any company fails in managing proper communication, it results in loss of trust in management, safety problem, bad customer service, and most importantly the loss of the support of key stakeholders at a time when that support is needed the most.

- **Limited Focus:**

In Conglomerate merger, if two organizations are from entirely different market and culture failure of integration is very high. In such cases focus gets blurred as new organization now has to work and focus on many units, and core competencies get weakened.

- **Failure to take Immediate Control**:

Control of the new unit should be taken immediately after signing of the agreement.
Most evidence suggests that mergers are more successful when merging firms make related products.

- **Failure of Leadership Role**:

Some of the roles leadership should take seriously are modeling, quantifying strategic benefits, building the case for M&A activity and establishing high standard for value creation. Walking the talk becomes very important during M&A's.

Conclusion

Due to globalization, liberalization and rapid technological change, business firms now face more competition from all around the globe. To face this competition, every business firm has to work very hard for profit maximization. For profit maximization, expansion of business is necessary and due to this change in business environment, mergers have become very popular over last 40 or 50 years .The main objective of merger is expansion and wealth maximization of shareholders in terms of synergy gain, increase in market share, better service to the customer and better financial and marketing advantages.

Along with financial aspects, it is very necessary to take care of cultural issues and employee issues of both firms for a successful merger. But due to lack of consideration of cultural issues and employee issues and giving more importance to economical gain and financial aspects many mergers result in failure. This eventually affects the customers and shareholders of both companies.

In this paper an attempt has been made to find the reasons of such failure, and there is no doubt that, cultural and people issue is one of them. Merger is not all about joining two companies or organizations but it means integration of two groups of people which are from different culture and mind-set. There is also a need to develop appropriate methodologies to effectively measure the performance of the mergers and their effects on the shareholders.

Utility & Future Work

Mergers continue to be a dominant growth strategy for companies worldwide. This is in part due to pressure from key stake holders vigilant in their pursuit of increased shareholder value. This study therefore timely identifies key factors which should be kept in mind while planning for successful mergers. This study uses semi-structured case studies to highlight major causes behind merger failures and evaluates the previous experiences in failed mergers in the last decade of 21st century. This study can be highly beneficial for those who want to learn from the past mistakes of other companies as one cannot afford to repeat the same mistakes.

Though I have tried to cover a lot in this paper but still a more detailed comprehensive study needs to be done keeping in mind the importance and usefulness of successful mergers in today's fast moving economy. Merger failure research has now been on-going for over 50 years. Despite this, there has been little change in failed merger rates over the same period. Even now more than 50% of the current mergers fail because of various reasons. So, some steps can be taken to reduce this shocking failure rate like –

1. Executives need to play more sincere and positive role in merged firms with a motive of value-maximization.
2. The various research studies done in this field should reach the business community so that, the business community can learn from this research and pursue it in their firms.
3. We need to look out for clear reasons and solutions to merger failure. Better quality research still needs to be done to solve this major strategic failure.

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