SMES VERSUS LISTED COMPANIES: ON EQUAL FOOTING WHEN CONFRONTED WITH A MERGER AND ACQUISITION ORGANIZATIONAL CULTURE INTEGRATION CHALLENGE?

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Abstract

Mergers and acquisitions (M&As) have been considered as the strategy of choice by large listed companies aiming to grow, diversify, achieve economies of scale or gain a competitive advantage. Recently, scholars and practitioners have shown a growing interest in assessing the human or cultural facets of M&As in an attempt to uncover factors, processes and behaviors that lead to successful post- merger or acquisition organizational cultural integration. This study examines the elements having the greatest impact on the success or failure of M&As in the context of non-listed SMEs, an area that remains largely understudied in the academic literature. Findings suggest that their success is largely based on respect for the existing pre-merger cultures and are not as dependent on the merger of organizational cultures as they are in large listed companies.

Keywords: merger, acquisition, organizational culture integration, non-listed SMEs

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Introduction

While mergers and acquisitions (M&As) have been common corporate practice for more than a century, the key determinants for their success as well as their failure remain poorly understood. M&A is understood in the current study as (1) a merger representing the consolidation of two entities into a single organization or (2) an acquisition, i.e. a purchase of a target company by an acquiring firm in which the latter controls the former. Although the term ‘merger’ generally refers to a ‘merger between equals’, this is rarely the case, as sooner or later there will be a ‘controlling’ organization and an organization ‘under control’.

Organizational culture “tends to be unique to a particular organization, composed of an objective and subjective dimension, and concerned with tradition, and the nature of the shared beliefs and expectations about organizational life” (Buono, Bowditch, and Lewis, 1985, p.

482). Subjective culture refers to shared values, norms, roles and beliefs among a firm's members, whereas objective culture is characterized by "artifacts" such as premises or office location, created to reflect the material aspect of culture. In an M&A process this 'unique organizational culture' of the merger- or acquisition- initiating company may potentially conflict with the culture of the company that it is merging with or acquiring.

The classification as to what exactly a large or small and medium enterprise (SMEs) is differs between the European Union (EU) and the Unites States of America (US). A company must employ at least 500 workers to be classified as "large" in the US, while in Europe 251 workers would suffice to be considered as a large company. In terms of SMEs, in European they are classified as (1) Micro firms (less than 10 employees and 2 million euros of sales volume or a total balance sheet less than € 2 million), (2) Small firms (10 to 50 employees, sales volume of € 2 to 10 million or a balance sheet total of €2 to 10 million) and (3) Medium firms (50 to 250 employees, sales volume of €10 to 50 million or a balance sheet total of €10 to 43 million). In the US, the Small Business Administration (SBA) defines small firms as entities with no more than 500 employees for most manufacturing and mining industries, and no more than $7 million in average annual receipts for most non-manufacturing industries. Across the 28 EU-member states, SMEs in the non-financial business sector employed 88.8 million people and generated €3.6 trillion worth of goods and services (EC annual report on European SMEs 2013-2014). In the US, the National Small Business Association (NSBA, 2014) claims that small employers comprise 99.7 percent of all employer firms in the U.S. and employed 50% of all Americans in the private workforce.

The most renowned US index for small-capitalizations, Standard & Poor's SmallCap 600®, otherwise known as the S&P 600, measures the small-cap segment of the U.S. equity market and incorporates firms with a market capitalization of between US$ 400 million and US$ 1.8 billion. The S&P 600's annual return in 2014 was 5.76%. In terms of the long-term performance of the index, it provided an annualized return of 9.02% over 5 years and a 5.05% annualized return over 10 years. As for Europe, Allianz Global Investors, a worldwide asset management fund, in October 2013 published a breakdown of European market capitalizations. It showed that 4,815 small cap stocks represented an overwhelming 93.5% of all listed firms, but accounted for only 20.1% of total market capitalization. According to Thomson-Reuters, in 2014 the total value of announced Small-Cap M&A deals, for companies with a market capitalization of up to $50 million, was over US$141 billion, a 17.2% increase year-on-year. However, the value of the small-cap M&A segment represented only 4% of all M&A transactions, and, accordingly, does not get much media coverage or provoke great academic interest. As a matter of fact, theories and models associated with M&As have been developed almost exclusively from the study and analysis of large deals between large firms (Weitzel and McCarthy, 2011).

The following sections provide a literature review on the meaning and main features of M&A, SMEs and organizational culture, present the methodology used in the exploratory study and conclude with a discussion of the findings.

1 Key success and failure factors associated with M&As

During the past three decades, the failure and success of M&As carried out by large, and especially listed, companies have been covered extensively by the media. The success of Shell and Royal Dutch Petroleum, Disney and Pixar, JP Morgan and Chase, Exxon and Mobil cannot offset the failure of Alcatel and Lucent, Daimler and Chrysler, AOL and Time Warner, News Corp and MySpace or Nokia and Siemens Networks.

M&A failure rates vary according to scholars, practitioners and other media bodies. It is estimated that merely half of all M&A meet initial financial expectations, with 50-60% resulting in failure (Cartwright and Schoenberg, 2006). Weber, Tarba and Öberg (2014) pointed out that the 83% of companies failed to achieve their merger goals, discussing the different factors that lead to such a low rates of success. And yet the rate of M&A deals shows no particular sign of lessening, even after the economic downturn of 2008 and 2009. According to Thomson-Reuters (2014), the number of announced M&A deals globally was valued at US$ 3.5 trillion in 2014, the strongest annual increase (47%) in corporate transactions since 2007. The total number of announced deals went from 36,800 in 2013 to 40,462 in 2014, representing a 6% inter-annual increase. M&As continue to be perceived by listed companies as the best strategy for enhancing their competitive advantage through expanding activities into new geographical zones, accessing new customers, enlarging product portfolios or incorporating new technologies and skills.

The available literature emphasizes multiple factors which lead to M&A failures, the first and foremost being related to unsuccessful cultural integration of different pre-merger (or pre-acquisition) organizational cultures. This deficiency may take several forms, such as: (1) lack of leadership support (2) inconsistent organizational culture assessment (3) lack of compatibility between organizational cultures (4) poor communication and lack of trust, as well as (5) lack of skills and management experience.

Hofstede (1983) paved the way for studies on the influence of national cultures on M&A success or failure by laying down the foundations of the theories of ‘cultural distance’ and ‘cultural relativity of organizational practices’. Notably, the study of M&A’s intercultural cultural dynamics and its impact on the post-M&A integration process gained particular weight in the academic literature (Cartwright and Schoenberg, 2006). Rottig, Reus and Tarba (2013) compared findings of 84 studies published in 40 different academic journals from 1980 onwards, representing more than thirty years of research on the impact of national culture on M&As. They shed light on a certain level of inconsistency and contradictory results in terms of (1) national cultural dimensions that do not seem to significantly affect the outcome of M&As (2) both negative and positive relations exist between intercultural distance and M&A performance. Failure patterns occur when the cultural component of the M&A is relegated to a lower priority than financial, operational and strategic issues. Several interculturally bound constructs have been investigated, again mostly within large listed firms: (1) acculturation process and acculturative stress (Larsson, and Lubatkin, 2001); (2) intercultural compatibility (Cartwright and Cooper, 2006); (3) intercultural distance (Hofstede, 1983); (4) intercultural clash, shock or gap (Larsson, and Lubatkin, 2001); (5) intercultural and organizational fit or compatibility (Chatterjee, Lubatkin, Schweiger, and Weber, 1992).

The corpus of academic literature regarding non-listed SMEs’ behavior and performance is rather limited (Bauer, and Matzler, 2014; Friedman, Carmeli, Tishler, and Shimizu, 2015; Rottig, Reus, and Tarba, 2013). Weitzel and McCarthy (2011) consider that the fact that SMEs do not usually provide information as to their general activities makes it virtually impossible to collect secondary data regarding their post-M&A performance. A study by Arvanitis and Stucki (2015) demonstrated positive and statistically significant performance effects for companies that acquired one or several SMEs. Weitzel and McCarthy (2011) found that, when involved in a M&A, non-listed SMEs: (1) are more motivated by value-enhancing objectives than larger firms, as their deal completion likelihood is 2/3 lower as compared to their large listed counterparts, since their smaller size and management structure give them a higher flexibility and likelihood to withdraw from value-destroying deals, (2) pursue external growth opportunities with a greater intensity than large listed organizations, and (3) are more likely to be financed with equity rather than debt, while the reverse is the norm in the case of M&As between large listed companies.

This study seeks to further explore the underlying factors of successful SMEs post-M&A organizational culture integration.

2 Methodology & Findings

Eighteen semi-structured interviews were conducted with French CEOs of non-listed SMEs. The firms were involved in forty-two national, cross-border and/or international M&As in various industries, e.g. software, automated material handling, intralogistics solutions, chemicals, construction, and real estate management. The interviews were conducted by phone as well as in person, and were based on a semi-structured question-guide. The interviews were audio-recorded, transcribed and analyzed. Some quotes from the transcripts are provided below.

Interviewees were confronted with a set of six-point numeric rating questions in order to respect a funnel-shape structure of the interview (Saunders, Lewis, and Thornhill, 2009). Respondents were asked, on a 5-point Likert-style rating scale, how important they considered 6 factors/variables which have been extensively cited in the literature for their role in the success or failure of a M&A. Here below are the responses given by the interviewed CEOs:

Tab. 1: 5-point rating scale with CEOs appreciation of the 6 key success factors

Degree of importance	1 Not at all	2 Somewhat	3 Moderately	4 Very	5 Extremely
1. M&A strategic vision				16	2
2. Deal structure		2	6	9	1
3. Due diligence process			2	14	2
4. Pre-M&A planning		6	8	4	
5. Post-M&A integration					18
6. Intercultural organizational management		12	4	2	

The findings reveal that the post-M&A organizational culture integration between acquiring and acquired SMEs is the *sine qua non* condition for achieving successful performance from the organizations that result from M&As. The post-M&A integration in terms of capability and know-how transfer between the acquired and acquiring entities was considered of primary importance by the interviewees. They considered that a successful integration requires specific competences in terms of the organizational change management, with, surprisingly, cross-cultural management skills being deemed as less important. The fundamental notion of mutual respect seems to be the corner stone of a M&A's success. As one of the interviewees puts it, "*Never forget that we are considered as potential intruders. As long as we are aware of that, we are compatible with all the other cultures*". The interviewed managers claimed to have achieved positive transformational post M&A change by placing human capital at the heart of the process, treating people with respect, genuinely trusting them and thus placing them in the best position to realize a successful M&A.

Consistent with Weitzel and McCarthy's study (2011), M&As in this research are deemed as being an important growth strategy instrument. Half of the interviewed CEOs mentioned that an acquisition is a strong growth catalyzer, in that an acquired firm tends to be well established in the market and that two thirds of the acquisitions cited were motivated by the interviewed CEOs' wish to merge with or to acquire firms that would give them access to a larger customer base on a national market and/or overseas. This finding is however at odds with the general M&A literature which proclaims that the primary purpose of these transactions is to ensure shareholder returns (Rani, Yadav, and Jain, 2015; Sirower, 1997). Moreover, it is important to note that 33 out of 42 M&As were qualified as successes by the interviewed CEOs, which again is at odds with previous cited M&A failure rates of 50 to 60 percent for listed companies. The much higher success rate of post-merger cultural integration for non-listed SMEs as opposed to large listed companies would be worth investigating in order to determine their "recipe for success" in the hopes of, one day, sharing best practices with their larger counterparts.

Perhaps the major limitation to this study is linked to the small number of interviewees. However, it is worth noting that the multiple M&A experiences of each CEO may mitigate the above mentioned limitation. Moreover, given the originality of the study, represented by the attempt to examine the role of organizational culture from the perspective of SMEs, largely ignored in the academic research to date, further qualitative research could complement these findings and substantiate their validity among a larger sample of SMEs. Future studies may wish to combine different levels of analysis (organization type, M&A transaction, industry domain, integration practices, etc.) in an attempt to better capture the dynamics of the M&A process and in fine elaborate a SME-focused framework for decision-making.

3 Conclusion

The results of the exploratory research, corroborated by the main findings of the literature review, reveal that non-listed SMEs' M&A success regarding cultural integration is based upon the acceptance of differences. It is promoted by a shared belief that fostering employee commitment, creativity and autonomy in post-M&A projects allows for mutually beneficial interactions between the acquiring and the acquired entities. This process does not require strict anticipation and pre-M&A planning, but imperatively needs to be nimbly and effectively managed in the post-M&A stages. In the particular case of the non-listed SMEs studied in this paper, M&A performance is supported by a few but nevertheless crucial elements which certainly deserve further investigation in order to be generalized: respect for cultural differences, commitment towards people empowerment, leadership's role in modeling and coaching actions and, last but not least, collaborative construction of the desired state of the combined organization from both a strategic and operational perspective. Thus, successful management of cultural aspects in the post-integration process turns out to be more a matter of a pragmatism and common sense related to CEOs' leadership style, vision and perception of the human asset of their firms. All synergistic gains and therefore the success of the M&As under study depend largely on the way the CEOs have led the change process towards the achievement of the initial objective.

The real difference, and at the same time the supreme force, of non-listed SMEs engaged in M&As is that these firms, thanks to their limited size, can place their human capital at the very heart of the process and thus manage individuals instead of business units. Their size may be perceived as a weakness on a capital market, but this feature is also a tremendous asset, when compared to large listed firms, which by their very nature are compelled to place shareholder return on investment as the most important success factor in the M&A process. Thus, a non-listed SME's ability to put people at the heart of their M&A growth objective, by empowering and valuing them, allows them to achieve sustainable results, ensuring both economic growth and employee retention and satisfaction.

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