

RESOURCE CONFIGURATION AND VALUE CREATION

FOLLOWING MERGERS AND ACQUISITIONS

by

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ABSTRACT

Mergers and Acquisitions (M&A) continue to be a popular vehicle for corporate profitability and growth. Although a rich stream of theory and research exists on M&A, there is considerable diversity in the findings and no consistent evidence validating the role of M&A in improving firm performance (e.g., Datta, Narayanan, and Pinches 1992; Haspeslagh and Jemison 1991; King et al. 2004; Ravenscraft and Scherer 1987). This apparent disconnection leaves open the possibility that a broader set of factors, beyond the constructs typically studied, may influence the outcome of M&A. Consequently, there is a recognized need for research to identify a theoretical framework that can help explain M&A performance.

M&A, as a vehicle to access and integrate assets and capabilities that exist outside the firm's boundaries, can be a promising field of study in marketing. Surprisingly, it has received relatively limited attention from marketing scholars. Likewise, research on M&A has been mute on related marketing issues. Against this backdrop, the central thesis of this dissertation is to adapt a marketing perspective and explore additional theories to provide insights into a new set of determinants to explain M&A performance. Within the purview of resource-based view of the firm (Barney 1991; Wernerfelt 1984), I elaborate and empirically assess the link between the resource configuration of the merging firms and M&A performance and also delineate the contingent factors that enhance or mitigate these effects. Specifically, I investigate how the strategic emphases of the merging firms facilitate merger performance. In this research, I define

strategic emphasis as the relative emphasis a firm places on building either brand resources or R&D resources (Mizik and Jacobson 2003). In this process, I examine whether M&A performance is a function of similarity or complementarity in strategic emphasis between merging firms.

There are conceptual and analytical arguments supportive of both resource similarity (e.g., Ansoff 1965; Hitt et al. 2001; Montgomery and Hariharan 1991) and complementarity (e.g., Harrison et al. 1991, 2001; Hoskisson and Busenitz 2002) as a positive driver of performance. The lack of a definitive answer is critical. I advance a contingency perspective based on merger motive to systematically explain the competing arguments. Much previous research has focused only on the main effect view of merger motives. I use two broad classifications: *Consolidation-based M&A* and *Diversification-based M&A*, and examine how each interacts with similarity and complementarity in the strategic emphases of the merging firms. I suggest that when there is similarity in strategic emphasis alignment, value creation is enhanced under the consolidation motive. Alternatively, for complementarity in strategic emphasis alignment, value is enhanced when the merger motive is one of diversification.

I use forward-looking financial market-based measures to evaluate M&A performance. Using stock market reactions to merger announcements, I examine synergistic gains accruing to the merging firms and wealth creation for the acquiring firms. The analysis draws from M&A announcements in two different industries that took place over the 22 year period between 1980 and 2001. Empirical tests considerably support the model's prediction; the findings point to the distinct role of resource configuration of merging firms, as well as to important interactions between resource configuration and motives. The findings provide practical insights into how firm-specific factors affect M&A performance. I discuss the implications of these results for

research on marketing's role within a firm and set a theoretical and empirical basis for future research on firm specific resources and M&A performance.

TABLE OF CONTENTS

PREFACE.....	ix
1. CHAPTER ONE: OVERVIEW.....	1
1.1. Introduction.....	1
1.2. Key Contributions.....	2
1.3. Empirical Context.....	4
1.4. Organization.....	5
2. CHAPTER TWO: THEORETICAL BACKGROUND.....	6
2.1. Overview of RBV.....	6
2.2. Firm Resources.....	9
2.2.1. Marketing Resources.....	11
2.2.2 R&D Resources.....	11
2.2.3 Linking Marketing and R&D.....	12
3. CHAPTER THREE: CONCEPTUAL FRAMEWORK AND HYPOTHESES.....	15
3.1. Outcome Variables.....	15
3.2. Strategic Emphasis Alignment: Similarity versus Complementarity.....	17
3.3. Merger Motive.....	20
3.4. Strategic Emphasis and Merger Motive.....	23
4. CHAPTER FOUR: RESEARCH METHODOLOGY.....	25
4.1. Event Study Methodology.....	25
4.2. Empirical Setting.....	28
4.3. Data and Sample Collection Procedure.....	29
4.4. Measures.....	30
4.4.1 Dependent Variables.....	30
4.4.2 Independent Variables.....	30
4.5. Approach to Analysis: Model Specification and Estimation.....	31
5. CHAPTER FIVE: RESULTS.....	33
5.1. Descriptive Statistics.....	33
5.2. Test of Hypotheses.....	34
5.2.1 Electronics Industry Results.....	35
5.2.2 FPC Industry Results.....	36
5.2.3 Post-Hoc Analysis.....	38
5.3. Additional Analysis.....	45
6. CHAPTER SIX: SUMMARY AND CONCLUSIONS.....	47
6.1. General Discussion.....	47
6.2. Implications for Theory Development.....	50
6.3. Implications for Practice.....	52
6.4. Limitations and Future Research.....	54
6.5. Conclusions.....	56
7. BIBLIOGRAPHY.....	71

LIST OF TABLES

Table 1 Operationalization and Sources of the Key Constructs	57
Table 2 Descriptive Statistics and Correlation Matrix: Electronics (N = 97).....	58
Table 3 Descriptive Statistics and Correlation Matrix: FPC (N =102).....	58
Table 4 Multiple Regression Results : Electronics	59
Table 5 Multiple Regression Results: FPC	60
Table 6 Post-hoc Probes of Three-way Interactions	61
Table 7 The Impact of Strategic Emphasis Alignment on Accounting Costs (n=75)	62

LIST OF FIGURES

Figure 1 The Conceptual Model	63
Figure 2 Acquirers' Cumulative Abnormal Returns (CAR): Electronics.....	64
Figure 3 Targets' Cumulative Abnormal Returns (CAR): Electronics	64
Figure 4 Synergistic Gains from the Merger: Electronics	64
Figure 5 Acquirers' Cumulative Abnormal Returns (CAR): FPC.....	65
Figure 6 Targets' Cumulative Abnormal Returns (CAR): FPC	65
Figure 7 Synergistic Gains from the Merger: FPC	65
Figure 8 Synergistic Gains under Consolidation Motive: Electronics.....	66
Figure 9 Synergistic Gains under Diversification Motive: Electronics	66
Figure 10 Acquirer Wealth under Consolidation Motive: Electronics	67
Figure 11 Acquirer Wealth under Diversification Motive: Electronics.....	67
Figure 12 Synergistic Gains under Consolidation Motive: FPC	68
Figure 13 Synergistic Gains under Diversification Motive: FPC.....	68
Figure 14 Acquirer Wealth under Consolidation Motive: FPC	69
Figure 15 Acquirer Wealth under Diversification Motive: FPC	69
Figure 16 Cost Efficiency under Consolidation: Electronics	70
Figure 17 Cost Efficiency under Diversification	70

PREFACE

This must be the most pleasant task in writing a dissertation. I take this opportunity to express my sincere appreciation to those individuals without whom I would not have reached this stage.

“It was the best of times, it was the worst of times....” This is the perhaps the most appropriate way to describe the last four years of my life. For various reasons, this was the most significant period of my life. So many people I have met and worked with and they have touched my life and changed it for a good measure.

I feel a tremendous debt of gratitude to my co-chairs: Prof. Vikas Mittal and Prof. Vanitha Swaminathan. They not only have been instrumental in guiding me throughout this exhilarating process, but also have taken a keen interest in my intellectual development and personal welfare. I am greatly appreciative of the constructive inputs and invaluable insights I received into my dissertation from the other committee members: Profs. Larry Feick, John Hulland, and Rajesh Chandy. I gratefully remember Profs. Rabikar Chatterjee, Jeff Inman, and R. Venkatesh for offering thoughtful advice and encouragement throughout my years in the program. It is difficult to express how much this program has added to my life. It has truly been a privilege to be around this set of wonderful people.

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1. CHAPTER ONE: OVERVIEW

1.1. Introduction

Mergers and acquisitions (M&A)¹ is a popular strategic option for firms seeking to expand (e.g., Porter 1987). It can be a faster and less risky means to access markets, products, technologies, resources and management talents compared to in-house developments. There has been explosive growth in the number and size of M&A transactions completed in recent years and the annual value of M&A now runs routinely in the trillions of dollars (Mergerstat 2003)². Despite their apparent popularity, nearly 60-80% of all mergers fail to create value (e.g., Christofferson, McNish, and Sias 2004; Dyer, Kale, and Singh 2004; Marks and Mirvis 2001).

While the topic of M&A has been examined broadly – particularly in the fields of finance, organizational behavior, and strategy – little consensus exists as to how they create value for firms. Some studies show that M&A enhances performance (e.g., Bradley, Desai, and Kim 1988; Lubatkin 1988; Malatesta 1983; Seth 1990a), while others suggest that M&A fails for a variety of reasons (e.g., Datta, Pinches, and Narayanan 1992; King et al. 2004; Porter 1987; Ravenscraft and Scherer 1987), including overestimation of synergies (Sirower 1997), lack of operational and financial synergies between merging entities (Montgomery and Singh 1984) and difficulties caused during the post-merger integration (Birkinshaw, Bresman, and Hakanson 2000, Gilson and

¹ Consistent with other research in this area, the terms “mergers” and “acquisitions” are used interchangeably to represent transactions where two firms combine to form a single entity.

² Merger volume in 2004, while lower than 2000’s record volume, is nearly 50% greater than that of 2003. Industry watchers believe that 2005 could see another increase of 15% to 20% (*BusinessWeek* 2005)

Black 1995; Homburg and Bucerius 2005). These mixed results represent an unsolved “puzzle” (Agarwal and Jaffe 2000) and offer inadequate insights into the determinants of an M&A’s success and failure (e.g., Bouwman, Fuller, and Nain 2003; Kaplan 2000).

M&A is one way through which a firm can enter a concentrated product market with substantial entry barriers (Yip 1982), thus gaining access to new resources that are not otherwise attainable on the open market (Hennart and Park 1993; Dyer and Singh 1998). The resource-based view (RBV) of the firm emphasizes firm-specific resources as a source of competitive advantage (Barney 1991, Penrose 1959; Wernerfelt 1984). Recent research in marketing has sought to examine mergers from a resource-based perspective (e.g., Capron and Hullan 1999; Homburg and Bucerius 2005). In the same spirit, this study builds on RBV to explore a hitherto unexplored set of determinants to explain M&A performance, provide new insights regarding the role of marketing, and offer normative criteria for target selection.

1.2. Key Contributions

This dissertation seeks to extend the present state of knowledge in three important ways.

First, I introduce the notion of *strategic emphasis alignment* as a critical construct influencing value creation following a merger. Given that a primary objective of many mergers is resource access (Dyer, Kale, and Singh 2004), I argue that searching for resource synergies between acquirers and their targets is fundamental to ensuring merger success. Mizik and Jacobson (2003) have suggested that a firm’s strategic emphasis (i.e., the relative emphasis that a firm places on marketing versus R&D) is strongly related to its valuation by the stock market. I extend this notion in the context of M&A and suggest

that *strategic emphasis alignment* (i.e. whether the strategic emphases of the target and acquirer firms are similar to or distinct from one another) is a key construct that captures synergy between merging entities and helps to explain value creation following mergers.

Strategic emphasis alignment, which captures the fit between acquirer and target based on their resource configurations, provides insights as to whether resource complementarity or resource similarity is more likely to result in value creation. There are mixed research findings regarding the impact of resource similarity and complementarity in an M&A context. Some researchers have suggested that resource similarity between acquirers and targets contributes to success. However, other research has argued that resource complementarity across merging firms is more likely to add long-term value (e.g., Harrison et al. 1991, 2001; Hoskisson and Basinet 2002). Based on the degree of strategic emphasis alignment between merging entities, I investigate the role of complementarity or similarity in a merger context and then extend the debate by proposing merger motive (consolidation or diversification) as a key moderator influencing the relationship between resource configuration and merger performance.

The second contribution pertains to the issue of how marketing resources (relative to R&D) influence value creation in the context of M&A. Recognition of the importance of marketing resources and their impact on firm performance is growing (e.g., Ramaswami, Bhargava, and Srivastava 2004; Slotegraaf, Moorman, and Inman 2003; Srivastava, Shervani, and Fahey 1998; Vorhies and Morgan 2005; Wernerfelt 2005). Yet, there is still little research on the role of marketing resources in an M&A context (for exceptions, see Capron and HULLAND 1999; Homburg and BUCERIUS 2005; Prabhu, Chandy, and Ellis 2005).

Third, while past merger research in marketing has typically used survey data, I utilize stock market reactions to merger announcements as a key dependent measure. Thus consistent with recent efforts in strategy research, this study utilizes ‘hard’ performance data rather than ‘softer’ measures. In doing so, I avoid concerns about poor response rates, common method bias, and memory and self-justification biases (Golden 1992; Kaplan, Mitchell, and Wruck 2000; Shimizu and Hitt 2005) associated with surveys. In addition, I link the firm’s marketing actions to financial performance by incorporating investors’ expectations of merger benefits. This adds to the recent stream of research on the marketing-finance interface (Srivastava, Shervani, and Fahey 1998; Lehmann 2004).

1.3. Empirical Context

The empirical setting of the study is based on the M&A completed across industries characterized by a high level of technological turbulence (i.e. Electronics) and a low level of technological turbulence (i.e. Foods and Personal Care) over a time period spanning twenty two years (1980-2001).³ These industries provide an interesting contrast to one another. Electronics industry is noted for technological intensity and firms primarily leverage their R&D resources in order to attain competitive advantage and superior long-term performance. On the other hand, in the FPC industry, firms typically rely heavily on brand and other marketing-related resources. This provides a better understanding of the role of different types of strategic emphasis and the degree of strategic emphasis alignment.

³ Deregulation has been a key driver of M&A activities and these three industries have not undergone substantial deregulation (e.g., Andrade, Mitchell, and Stafford 2001).

1.4. Organization

The thesis is organized as follows. The next section serves to summarize the general theory of RBV of the firm and how it provides the lens of the subsequent theory building. In addition, I review two focal firm resources and their interactions to lay the foundation of the study. In the third section, I present the conceptual framework and formulate the hypotheses. The research design, methodology used, and the operationalization of constructs appear in the fourth section. In the fifth section, I report the results of the empirical analysis. Following the discussion of results, I conclude by describing the implications of my results for marketing theory and practice, acknowledging the limitations of the study, and identifying areas for future research.

2. CHAPTER TWO: THEORETICAL BACKGROUND

Resource based view is the central theoretical perspective that I draw on to assess the combining potential of the merging firms, and as such, how firm specific resources play a potent role affecting M&A performance. RBV uses internal organizational resources to explain firm diversity and performance heterogeneity. I contribute to this tradition by developing and testing a framework that illustrates how merged firms can mobilize and deploy the combined resources toward higher valued uses. I also draw on aspects of relatedness theories in a merger context (e.g., Harrison et al. 2001; Singh and Montgomery 1987) and theoretical work in an intraorganizational context (e.g., Dutta, Narasimhan, and Rajiv 1999) to examine the impact of resource configuration on post-merger performance.

2.1. Overview of RBV

Widely held views of the industrial economics paradigm argue that external market forces primarily drive competitive advantage (Porter 1985; Rumelt 1984). In contrast, RBV employs an “inside-out” approach and tends to emphasize that the principal driver of a firm’s competitive strategy and performance is internal. Thus the firm is viewed as primary unit of analysis. This departs from the traditional economic theory on two counts: first, the focus is on heterogeneous firms, not homogenous firms, and second, the theory is about growth, not equilibrium. Tracing the origins of their work to Penrose (1959), resource-based theorists argue that the firm can be best viewed as a collection of resources and capabilities, and firms differ in their endowment of these resources and capabilities (Barney 1991; Wernerfelt 1984). These resources can be

physical, such as unique equipment or innovations protected by patents, or they can be intangible endowments, such as brand equity or operating routines. Thus, two firms cannot be alike because they will not have the same stock of physical and intangible assets and skills. Also, the strategic factor markets for those resources are inherently imperfect. Without such imperfections, firms could only hope for normal returns because above-normal returns would be competed away in the market. RBV proponents posit that the long-run profitability of the firm is closely associated with the growth in the productive opportunity of the firm.

Central to this perspective are two alternative notions: first, firms within the same industry may be heterogeneous with respect to the strategic resources they own and control, and second, these resources are not perfectly mobile across firms and thus heterogeneity can be long lasting. Broadly speaking, the approach provides some important insights into conditions leading to sustainable competitive advantage. For example, a firm should consider competing or entering into industries where its resources can be the key success factors and thus its competitors would be at a significant disadvantage. Consequently, the propensity to become disproportionate in the levels and stocks of a firm's resources and capabilities is the fundamental cause of interfirm performance variations.

Not all resources have the potential to contribute towards above normal returns and sustainable competitive advantage. Four specific conditions can exploit product market imperfections that create rent-producing potential. First, the resources have to be *valuable*, so that they aid a firm in formulating and implementing strategies to neutralize threats and exploit opportunities posed by the external environment. These resources

must contribute positively to the final offerings of the firm, and thus make a difference to the customers. Also, these resources bestow on a firm the ability to generate profit streams. For example, resources acquired at a price below the discounted net present value could lead to a long term advantage (Peteraf 1993).

Second, these resources cannot be possessed by a large number of current or potential competitors. Thus, these resources have to be *rare* in the sense that they must be in short supply relative to demand. This ensures that other firms cannot exploit these resources to implement their strategies. Scarcity in terms of resource functionality or utility, rather than resource type, is desired (Peteraf and Bergen 2003).

Third, these resources should be so firm-specific that they cannot be utilized outside of the firm and thus are difficult to sell owing to being *imperfectly mobile* or *imperfectly imitable* (e.g., Dierickx and Cool 1989; Lippman and Rumelt 1982; Peteraf 1993). This is related to the characteristics of the process by which these resources are accumulated. As these processes are created within the firm and embedded in organizational activities, these cannot be traded in the market, nor can they be observed readily from outside. Causal ambiguity or uncertainty regarding the causes of efficiency differences among firms prevents the imitation efforts of competitors and preserves the condition of heterogeneity (Dierickx and Cool 1989; Rumelt 1982). Thus a firm that has developed an advantageous research position is protected to the extent that its resources are bound to the firm for a long time, and are non-tradable and less valuable to other users. Furthermore, resources have tacit components and are specific to certain applications. In summary, the test of imitability can be sustained under three conditions: (1) when the resource is dependent on a unique historical condition (e.g., Ansoff 1965),

(2) when the link between resource and competitive advantage is ambiguous (e.g., Barney 1986), and (3) when the advantage generated by the resources is socially complex (Dierickx and Cool 1989).

The fourth requirement pertains to the lack of *substitutability*. To confer competitive advantage, there should not be any strategically equivalent resources available to competitors. The potential impact of a substitute product can reshape the industry. For example, the steel industry lost a major market in beer cans to aluminum makers in the 1980s. Resource bundles that are very dissimilar can also serve as strategic substitutes.

RBV of the firm has inspired a rich array of studies, ranging in several domains, including marketing strategy (e.g., Capron and Hulland 1999; Dickson 1992, 1996; Hunt and Morgan 1995; Ofek and Sarwary 2003). By examining the resource endowments and capabilities of merging firms with which they are deployed as sources of positional advantage, this study seeks to broaden RBV's range and strengthen its position as the dominant conceptual landscape of explaining firm performance in M&A.

2.2. Firm Resources

A wide range of views and definitions of resources has been put forth in previous research. Resources can take a variety of forms. For this dissertation, resources are defined as stocks of knowledge, skills, financial and physical assets, human capital, routines, and other tangible and intangible factors that a business owns and controls (Amit and Schoemaker 1993; Grant 1991). These resources enable a firm to perform its functional activities efficiently and effectively and to make superior value offerings. Consistent with the RBV, firms are seen as repositories of assets and capabilities,

accumulated in a firm-specific, path-dependent manner. Heterogeneity among firms in owning and controlling valuable, rare, inimitable and imperfectly mobile resources is the fundamental driver of performance and furnish the potential for sustaining competitive advantage (Barney 1991; Hunt and Morgan 1995; Lippman and Rumelt 1982; Mahoney and Pandian 1992; Peteraf 1993; Srivastava, Shervani, and Fahey 1998; Wernerfelt 1984).

The idiosyncratic nature of transaction-specific resources often precludes their tradability on open markets. Thus, acquisitions provide a key mechanism for businesses to acquire, exchange, or redeploy these tacit and organizationally embedded unique resources and to enhance learning that would otherwise not be possible. Firms acquire other businesses to extract value by putting newly acquired resources into productive use and by combining them with underutilized resources that they already own (e.g., Capron, Dussauge, and Mitchell 1998; Karim and Mitchell 2000; Vermuelen and Barkema 2001). Firms may have an internal incentive to acquire in order to realize benefits from exploiting overly abundant resource. Some resources have the potential to be deployed in many ways and multiple times. Also, a critical mass of resources can facilitate further resource accumulation (Dierickx and Cool 1989).

The focus of this research is on two specific resources, marketing and R&D and their interrelated roles in M&A performance. Both these resources are intangible and market specific, difficult to imitate and transfer, and typically do not appear on the balance sheet. The key managerial challenge is to deploy these two resources in an effective way so a firm can potentially apply these to beyond the industry of origin.

2.2.1. Marketing Resources These are the resource endowments the firm has acquired or built over a long time horizon and can be deployed to advantage in the market place. Marketing resources have been widely acknowledged as “market-based assets” (e.g., Srivastava, Shervani, and Fahey 1998) and “higher order resources” (Morgan and Hunt 1995) capable of generating future cash flows. These form an important subset of the resources that contribute to M&A performance (Capron, Dussuage, and Mitchell 1998). Marketing resources such as brand names are seen as important firm specific capital resource. A strong brand can lock-in loyal customers, who are less vulnerable to competition (Anderson and Sullivan 1993) and have high lifetime value (e.g., Rossiter and Percy 1997). It can convey information about product quality (Erdem 1998), reduce perceived risk and uncertainty (Montgomery and Wernerfelt 1992), increase distribution clout in the market place (Kamakura and Russell 1994) and deflect competitive initiatives (Srivastava and Shocker 1991). Brands can also serve as a foundation from which new products are launched. For example, a brand name with high equity can be extended to new product variants (Bergen, Dutta, and Shugan 1996) and new categories (Dacin and Smith 1994) without impairing its value. Further, investments in marketing can help a firm to appropriate value from innovations (Mizik and Jacobson 2003).

2.2.2 R&D Resources R&D resources pertain to the innovative and technological proficiencies of the firm and are tied closely with new product development skills. These are also recognized as higher-order resources that enable a firm to perform certain critical value-chain activities better than competitors (e.g., Porter 1985; Prahalad and Hamel 1990). Firms invest in new product efforts to create superior knowledge and capabilities, generate higher profit and enhance their existing competitive positions. Strong R&D

resources induce greater leader effort (Ofek and Sarvary 2003) and enable firms to become more proactive in exploiting external opportunities (Zahra and Covin 1993). Development of new products has been envisioned as a “higher order” or “dynamic” capability (Eisenhardt and Martin 2000; Teece, Pisano, and Shuen 1997) and is recognized as a primary means of corporate renewal (Danneels 2002). Likewise, Day (1994, p. 38) has described new product development as a “key firm capability involving complex bundles of skills and accumulated knowledge.” Compared to updated existing products, new products command higher financial values (Chaney, Devinney, and Winer 1991), and a higher level of innovation enhances a firm’s market value and profitability (Blundell, Griffith, and Van Reenen 1999; Wuyts, Dutta, and Stremersch 2004). Due to its often tacit nature and high asset specificity, a strong product development capability is difficult for competitors to imitate (e.g., Wind and Mahajan 1997). Prior research has shown that acquiring product development resources can allow firms to gain access to new knowledge, and reduce the costs and risks associated with developing new products and processes (Millson, Raj, and Wilemon 1996). As such, strong R&D resources of the target firm are often the primary motivation for a high technology acquisition (Ranft and Lord 2002). In the same vein, Wind and Mahajan (1997, p.7) state that “the increased complexity and cost of developing truly innovative products and advances in new technologies often require expertise that the firm does not have.”

2.2.3 Linking Marketing and R&D Prior research suggests that the linking of marketing and R&D capabilities can be instrumental in creating competitive advantage (Gort 1962; Lemelin 1982; Montgomery and Hariharan 1991) and exerting systematic influence on the market value of the firm (Hirschey and Weygandt 1985). R&D activities and

advertising efforts are described as “upstream capabilities” and “downstream capabilities” respectively (Caves 1996). Cooper (1979) reports a significant positive correlation between new product success and the level of a firm’s marketing resources, including advertising, distribution and sales force. The success of a firm is contingent on how quickly and efficiently it can come up with the new products and the ability needed to commercialize these to satisfy the consumer needs and preferences. Moreover, shortened product life cycles have forced companies to commercialize the technologies much faster than before. For example, in the semi-conductor industry, product lifecycles shrank by 25% in the 1980s (Iansiti and West 1997). Strong marketing capabilities will help to diffuse the innovation in the market place. Better understanding of the market, customers and competitors through marketing capabilities will help firms to come up with appropriate product breakthroughs and also to sustain these innovations. A strong marketing resource base builds awareness and stimulates the adoption rate of new products. In a similar vein, Robertson (1993) contends that reducing penetration time for a new product is as important as coming up with the new product in the first place.

Marketing scholars have dedicated considerable efforts to understand the interaction between marketing and R&D resources and how market knowledge is transferred to and integrated with technological knowledge (e.g., Dutta, Narasimhan, and Rajiv 1999; Gatignon and Xuereb 1997; Griffin and Hauser 1996; Moorman and Slotegraaf 1999; Ofek and Sarvary 2003; Olson, Walker, and Reukert 1995; Song and Parry 1997; Song et al. 2005; Sorescu, Chandy, and Prabhu 2003). In summary, this stream of literature has captured and suggested that linking of marketing and R&D

resources can enhance firm performance beyond their individual effects and create competitive advantage.

3. CHAPTER THREE: CONCEPTUAL FRAMEWORK AND HYPOTHESES

Figure 1 illustrates the conceptual framework that guides this study. The model suggests that the link between resource configuration and M&A performance is moderated by merger motive. In discussing this framework, I first describe the dependent constructs in more detail, and then turn to developing hypotheses and rationales that underlie the relationships summarized in the model.

[Insert Figure 1 here]

3.1. Outcome Variables

Consistent with recent developments in finance literature, my outcome variables are based on the stock market perceptions of M&A announcements. Returns to stockholders represent the market's unbiased expectations regarding M&A performance and provide an assessment of discounted future cash flows. Efficient capital market theory (e.g., Fama 1970) holds that stock prices adjust instantaneously to new information and thus reflect long-term investor expectations about the cash-generating ability of a business. It is forward-looking and reflects the capital market's overall unbiased assessment of the present value of the future cash flows to shareholders (Rappaport 1987).

Synergistic gains and *acquirer wealth* serve as my two dependent variables.⁴ The synergistic gains reflect longer-term consequences of M&A for the combined firm and are based on the abnormal return accruing to both the target and the acquirer following the merger announcement. It captures the investors' belief regarding the extent to which

⁴ Synergistic gains and acquirer wealth are highly correlated as the latter is included in the conceptualization of synergistic gains. Detail follow in section 4.

the target and acquirer firm can be run efficiently such that the value of the merged entity exceeds the sum of the values of the two combining firms operating on their own (Bradley, Desai, and Kim 1988; Seth 1990a). Thus I posit that value creation in M&A depends on the combination of the characteristics of the two merging firms, rather than the characteristics of each of the firms considered alone.⁵ By looking at the total return (the return to a value weighted portfolio of the acquirer and target) at the time of merger announcement, I address the question of whether the market believes it is value-enhancing.

The second dependent variable is the level of acquirer wealth creation following the merger announcement. With the growth of options as a form of managerial compensation in the 1990s, managerial wealth is tied closely to stock prices. There is considerable empirical evidence that M&A is a mixed blessing for the shareholders of acquiring firms. In sum, there is no clear value creation in the sense of earning returns significantly in excess of the opportunity cost of capital. Some researchers report slightly positive or neutral returns to acquirers (Asquith, Bruner, and Mullins 1983; Bradley, Desai, and Kim 1988; Leeth and Borg 2000; Mandelker 1974), whereas, other studies document significantly negative returns (e.g., Houston, James, and Ryngaert 2001; Mitchell and Stafford 2000; Moeller, Schlingeman, and Stulz 2005; Morck, Schleifer, and Vishney 1990). Under the light of these ambivalent findings, wealth creation of acquiring firms remains conceptually appealing and managerially relevant to study.

⁵ Acquisition involving positive synergy may also mean that the loss of value for the acquiring firm is more than offset by the gain of the acquired firm (Bradley, Desai, and Kim 1988).

3.2. Strategic Emphasis Alignment: Similarity versus Complementarity

Following Mizik and Jacobson (2003), I define a strategic emphasis as the relative resource commitment and management attention a firm places on R&D relative to Marketing. As such, strategic emphasis in R&D means that firm's allocation of resources is made primarily to R&D. Focusing on R&D creates superior knowledge and technological capabilities leading to improved product quality and performance. Innovation becomes a focal point of competition and firms satisfy the changing needs of customers by generating highly innovative and superior products. This requires substantial investment in developing new product platforms, channels, and market segments. In contrast, a *strategic emphasis in marketing* occurs when a firm chooses to allocate its resources primarily to marketing activities. This entails differentiation from competitors and creates positional barriers through brand and image building, marketing communication, and promoting consumer adoption of its offerings.

M&A performance depends on whether the firms can creatively combine and leverage their pooled resources to achieve novel and rent-generating competitive market outcomes (e.g., Capron and Hulland 1999; Homburg and Bucerius 2005). I explore the trade-off between two contrasting strategic choices available to firms: creating value versus appropriating value. Value creation influences the potential magnitude of the advantage or surplus firms create; whereas, value appropriation influences the amount of advantage or surplus that the firm is able to capture. This view draws on market-focused theories of exploration and exploitation (e.g., March 1991). Exploration strives on creating new knowledge and skills; whereas, exploitation primarily involves improving skills and procedures associated with current market segment and associated marketing mix (Kyriakopoulos and Moorman 2004).

Resource similarity or complementarity is often operationalized using proxies such as firm size (Baum and Korn 1996) and strategic group membership (e.g., Gimeno and Woo 1996). My conceptualization of the construct is based on the strategic emphases of the merging firms. Similarity in strategic emphasis exists when the two merging firms have same strategic emphasis, i.e., marketing or R&D. Complementarity in strategic emphasis, on the other hand, is the context where the merging firms differ in their strategic emphasis.

Previous research has yielded an extensive literature, much of which supports the view that relatedness facilitates organizational integration, and thereby helps the firm realize potential synergies (Chatterjee 1986; Hitt et al. 2001; Larsson and Finkelstein 1999). This can enhance M&A performance in three ways. First, mergers involving firms with similar strategic emphases are better able to harmonize processes and pool similar resources following a merger. Such pooling is likely to result in greater economies of scale both in production and distribution, leading to reduced costs and superior post-merger performance (Chatterjee 1986; Lubatkin 1983). For example, when both firms possess strong brands, such unions can form brand alliances (e.g., Shocker, Srivastava, and Reukert 1994) or co-branding (Reddy, Holak, and Bhat 1994). Likewise, higher level of in-house R&D capabilities and understanding can improve the ability to appropriate value from an acquired technology that is complex (Chatterjee and Wernerfelt 1991; Deeds 2001; Veugelers 1997; Makadok 2001). Second, mergers involving firms with similar strategic emphases facilitate marketing, task, and organizational integration (Homburg and Bucerius 2005; Pablo 1994; Shrivastava 1986), and allow firms to broaden their relationships with existing customers (Capron and Hulland 1999;

Srivastava, Shervani, and Fahey 1998). Consider the recent acquisition of Gillete by P&G. Both firms have strong marketing resources, and it is expected to give more power to P&G to negotiate advantageous deals with media companies and retailers. Finally, mergers involving strategically similar firms are more likely to share similar norms and values. Such shared norms and values have been found to contribute extensively to merger success (Birkinshaw, Bresman, and Hakanson 2000; Nahavandi and Malekzadeh 1988; Sales and Mirvis 1984).

In contrast to the preceding position, some researchers have argued that superior performance gains can be attained through the integration of complementary resources (e.g., Barney 1988; Capron and Pistre 2002; King, Covin, and Hegarty 2003; Larsson and Finkelstein 1999). Complementarities can be valuable as the interaction of the parts increases firm efficiency and have been described as “cospecialization” (Teece 1988) and “interconnectedness” (Dierickx and Cool 1989). Within the merger context, it can influence value creation through several different mechanisms. First, firms seek complementary resources to compensate for their own resource deficiencies. This does not duplicate existing resources but adds value to a firm’s existing resources (King, Covin, and Hegarty 2003). Existing resources are better utilized in conjunction with the complementary resources of the target. For instance, firms with strong marketing resources may acquire product development resources to gain access to new knowledge, and reduce the costs and risks associated with developing new products and processes (Millson, Raj, and Wilemon 1996). Second, complementarities can increase firm efficiency (Walker and Reukert 1987). For example, Teece (1986) argues that firms in high-growth industries seek partners with complementary capabilities to facilitate the

timely introduction of new products. Third, the contribution of complementary resources can reduce organizational friction during the integration phase of merger implementation, minimizing the need to eliminate redundant resources.

Drawing on these two divergent streams of thoughts, conflicting predictions emerge. The ambivalent results from previous research make it worthwhile to address the theoretical tension. The following are the competing hypotheses.

H1_a: Similarity in strategic emphasis between the merging firms, when compared to complementarity, will lead to the (a) greater synergistic gain and (b) greater acquirer wealth creation following merger announcements.

OR

H1_b: Complementarity in strategic emphasis between the merging firms, when compared to similarity, will lead to the (a) greater synergistic gain and (b) greater acquirer wealth creation following merger announcements.

Further theoretical development can be aided by delving into the systematic factors that influence the impact of the similarity and complementarity of resources on merger performance. Past literature has not provided definitive prescriptions on this issue and it is my contention that these apparently contradictory perspectives can, in fact, be reconciled with one another by considering the motive underlying the merger. Before turning to a discussion of how strategic emphasis alignment and merger motive interact to affect performance, I first detail the main effect of motive.

3.3. Merger Motive

Mergers can be driven by a complex pattern of motives and each of the transactions can be different (e.g., Bower 2001). Following Anand and Singh (1997), I use a broad

classification where the motive for pursuing M&A is either consolidation or diversification. Firms use consolidation-based mergers to strengthen or expand their positions in existing product markets. When firms within the same industry merge, gains in market power may result (e.g., Chatterjee 1986; Montgomery 1985; Stigler 1964), enabling the merged firms to eliminate less efficient management, achieve economies of scale, charge higher prices, achieve higher distribution clout, offer greater product variety, and reduce competitive activities. For example, in the acquisition announcement of Sears by Kmart, the combined company expects to save \$300 million a year through “improved merchandising and non-merchandising, purchasing scale, as well as improved supply chain, administrative and other operational efficiencies” (*Dow Jones Newswire* 2004).

Merging firms may also be able to increase their bargaining power over suppliers by pooling their purchasing and forcing suppliers to compete on a price basis (Fee and Thomas 2004). Furthermore, production, marketing, and distribution efficiencies can be achieved leading to lower costs and greater operational synergies (Chatterjee 1986). Corporate performance is found to be higher for firms that have diversified into technologically related industries than those that have diversified into technologically unrelated industries (Robins and Wiserama 1995).

On the other hand, firms can use diversification-based mergers to expand into unrelated businesses and leverage the excess resources. Consistent with RBV, resources are subject to market failure and managers can apply those resources to new products through diversification. Historically, the drive to move into unrelated lines of business was motivated in part by strong antitrust enforcement, which was relaxed in the 1980s (Shleifer and Vishny 1991). General Electric and Walt Disney are good cases in point.

Through a pattern of different acquisitions, General Electric has become a diversified conglomerate with operations in insurance, television broadcasting, medical equipment, and plastics. Similarly, Disney has entered in feature films, books, records, cable TV, retail stores and the National Hockey League franchise.⁶

A diversified firm can minimize both its industry-specific and its overall business risk (Berger and Ofek 1995; Donaldson and Lorsch 1983) and enjoy efficiency from accessing internal capital market (e.g., Stein 1997). It can also gain from economies of scope between successive stages of production (Wernerfelt 2005). By entering a new line of business, the firm increases market share through geographic extension and new products, leading to higher margins and customer loyalty across product categories (Anand and Shachar 2004).

A broad range of commentaries and analyses, based on different time periods, has shown that costs of diversification most often outweigh its benefits (e.g., Anand and Singh 1997; Denis, Denis, and Sarin 1997; Lamont and Polk 2002; Montgomery 1985; Morck, Shleifer, and Vishny 1990; Palich, Cardinal, and Miller 2000; Rumelt 1982)⁷ and many unrelated acquisitions are later divested (e.g., Ravenscraft and Scherer 1987; Kaplan and Weisbach 1992). Likewise, market values of diversified firms have typically been found to be lower when compared to stand-alone firms (Berger and Ofek 1995; Lang and Stulz 1994; Montgomery and Wernerfelt 1988; Rajan and Servaes 2000)⁸. The agency view describes that managers of acquiring firms embark on diversification to maximize their own utility at the expense of the shareholders (e.g., Amihud and Lev

⁶ While this has been a successful strategy for GE, it did not work that well for Disney.

⁷ For exceptions see Elgers and Clark 1980; Lubatkin 1987

⁸ There has also been an argument that firms diversify because they trade at discount (e.g., Graham, Lemmon, and Wolf 2002; Gort, Grabowski, and McGuckin 1985)

1981; Jensen 1986). Diversification stretches the acquiring company's management skills, and potential efficiencies and internalizing transactions may not overcome the bureaucratic costs. Thus:

H₂: A consolidation motive, when compared to a diversification motive, will lead to (a) greater synergistic gains and (b) greater acquirer wealth creation following a merger announcement.

3.4. Strategic Emphasis and Merger Motive

As argued in the previous section, the merged entity is likely to enjoy increased market power and greater economies of scale when pursuing a consolidation-based merger. A merger occurring in the same industry will promote specialized learning and there will be a reduced need for extensive planning and coordination. Furthermore, when the strategic emphases of the acquirer and the target are similar, there is greater potential for the acquirer to productively leverage its pre-existing resources, "dominant logic," and critical success factors across multiple markets (e.g., Prahalad and Bettis 1986). Thus, the combined firm will find it easier to realize the potential gains of consolidation through integration when the strategic emphases of the two firms are aligned than when they are distinct. Also, it becomes easier to achieve scale economies and operational synergies through combining similar resources and operations. Additionally, the shared norms and values make it easier to set strategic priorities following a merger and help to combine the cultures of the two organizations. Conversely, the need to integrate firms with different strategic emphases is likely to add coordination costs while also increasing the likelihood of cultural clashes (Birkinshaw, Bresman, and Hakanson 2000; Sales and Mirvis 1984).

Considerable cost reduction is also possible when the merger is focused on consolidation. I argued earlier that economies of scale accrue to mergers of firms within the same industry. Such economies of scale are likely to be accentuated when similar resource configurations are pooled following a merger. Specifically, combinations of similar (R&D or marketing) resources are likely to result in greater experience curve effects and enhance the cost reductions that follow consolidation.

In contrast, diversification-based mergers typically entail changes in administrative structures, systems, and other management processes. As firms move further from their core businesses, managers are less likely to have an intimate understanding of the new business, competitors' strategic moves, and other critical success factors. New know-how or specialist skills have to be acquired to extract gains from these acquisitions. Those are likely to be acquired from outside the firm, and can be embedded in contexts that differ from that of the acquiring firm (e.g., Chatterjee and Singh 1999; Zahra and George 2002). Under this context, attempts to funnel new activities through the existing resource chains will not be effective and may even hamper performance. However, under the similarity in strategic emphasis alignment, firms are more likely to use existing resource chains while neglecting less obvious sources of synergy. Thus, I posit that the successful deployment of firm-specific and imperfectly mobile resources across new businesses will be easier when there is complementarity in strategic emphasis alignment. For example, Hitt et al. (1993) found that when firms combined different products, markets, and know-how, they were able to enhance their overall success. This suggests that diversification may create opportunities to leverage existing products in new markets, sell new products in existing markets, and enrich

existing R&D knowledge, leading to multiple sources of revenue-enhancement. At the same time, similarity in strategic emphasis under the same industry may lead to overlapping resources and fewer opportunities for knowledge synergies. Summarizing:

H₃: A consolidation-based merger (diversification-based merger) under similarity in strategic emphasis alignment (complementarity in strategic emphasis alignment) will lead to (a) greater synergistic gains and (b) higher acquirer wealth creation following a merger announcement.

4. CHAPTER FOUR: RESEARCH METHODOLOGY

My market-based measure of merger success is forward looking, reflecting investors' expectations of the net present value of all future cash flows expected to accrue to the merging firms. It is an especially appropriate metric for capturing value creation in the context of an event (Kalyanaram, Robinson, and Urban 1995). I use an event-study methodology that reflects the future financial ramifications of an event. Specifically, it measures the magnitude of the effect that the event has on the expected profitability and risk of a portfolio of the firms. It is driven by the tenet that the share prices represent the present value of expected future cash flows to shareholders. This method is based on measuring the abnormal stock return – or the systematic change in the stock price – to shareholders in the period surrounding an event (e.g., merger announcement) relative to the average stock price level prior to the event, adjusted for general market movement.

4.1. Event Study Methodology

Modern theory of finance has developed a methodology to study the behavior of security values. The efficient market/rational expectation hypothesis (e.g., Fama et al.

1969; Fama 1970) posits that the stock price accurately reflects all public information related to the performance of the firm. Although a firm's profit can be influenced by several factors, isolating the contribution of any one of those factors is difficult. This is why I measure the abnormal stock return, which is the raw return less a benchmark of what investors required that day. Only the occurrence of an unanticipated event will cause a change in the firm's security price. The stock prices quickly adjust to new information and incorporate any changes in value that the M&A are expected to bring. The magnitude of the change should be an unbiased estimate of the value of changes to the firm's expected future cash flow (Brown and Warner 1985). Over the last few decades, the event study approach has been widely used in finance, accounting, and strategic management research. It has also been used to assess the ramifications of marketing-related events such as new product introductions (Chaney, Devinney, and Winer 1991), celebrity endorsement (Agarwal and Kamakura 1995), company name change (Horsky and Swyngedouw 1987), brand extensions (Lane and Jacobson 1995), and introduction of online channels (Geyskens, Geylens, and Dekimpe 2002). The details of the event study methodology are laid out below.

The methods used conform generally to the received methodology used widely in finance. The event study method compares the actual stock return on the event day for firm i with the return that would be expected if the event had not taken place [E (R_{it})]. The stock return is the percentage change in the stock price between time $t-1$ and t .

$$(1) \quad R_{it} = \frac{P_{it} - P_{it-1}}{P_{it-1}}$$

The expected return $E(R_{it})$ to firm i at time t can be described as a linear function of the returns from a benchmark portfolio of marketable assets R_{mt} . The benchmark portfolio in this case is the value-weighted market portfolio reported in CRSP for a given date.

$$(2) \quad E(R_{it}) = \alpha_i + \beta_i R_{mt}$$

The difference between the actual return and the estimated expected return provides a measure of abnormal return e_{it} for the shares of acquirer i at time t .

$$(3) \quad e_{it} = R_{it} - E(R_{it}) = R_{it} - (\hat{\alpha}_i + \hat{\beta}_i R_{mt})$$

Cumulative Abnormal Returns (CAR). The analysis is based on the excess return between the opening stock price the day before the announcement and the closing stock price the day after the announcement, that is, an event window of event day -1 (t_1) through event day +1 (t_2). Some merger announcements may have occurred after the close of the stock market, and that is why the possible effect of the day after is also taken into account. I also aggregate the abnormal returns over the event period (t_1, t, t_2) to obtain the cumulative abnormal return (CAR) as shown in equation 4. I compute the CAR for both the acquirer and the target separately.

$$(4) \quad CAR = \sum_{i=-1}^{i=+1} e_{it}$$

Synergistic Gains and Acquirer Wealth from Mergers. The synergistic gains from the mergers are calculated using the cumulative abnormal returns of the target and acquirer and calculating the wealth gains based on their respective market values of equity (MVE) as follows. The MVE is the number of shares outstanding multiplied by the share price of the firm in the year preceding the merger year. The wealth gains for both target and acquirer are then summed:

$$(5) \quad \text{Synergistic Gains} = [(CAR_{\text{acquirer}} * \text{Acquirer MVE}) + (CAR_{\text{target}} * \text{Target MVE})]$$

$$(6) \quad \text{Acquirer Wealth} = (\text{CAR}_{\text{acquirer}} * \text{Acquirer MVE})$$

4.2. Empirical Setting

The sample consists of all publicly disclosed M&A in the Electronics industry (SIC Code: 36) over the interval January 1991 to December 2000 and the Food and Personal care industries (SIC code: 20 and 28 respectively) over the interval January 1980 to December 2001.⁹ By modeling these industries, I get the opportunity to compare across the industries. This would not have been possible to obtain in a cross-industry study.

The nature of the primary industry within which the acquiring firm operates affects the value of its resources, and also affects the type of resources it seeks through M&A. Typically, firms will seek to acquire and control those resources that are most valuable for maintaining a competitively superior position (Barney 1991; Hunt and Morgan 1995). Because the Electronics and Food and Personal Care (hereafter FPC) industries do contrast significantly, there will be some variations in my study conditions. Electronics industry is highly dynamic, and is characterized by both high technological and high market turbulence. The scientific know-how plays a focal role and leading firms in the Electronics industry (e.g., Sony, Motorola) use their strong R&D resources to support continuous innovation. On the other hand, FPC industry is relatively mature, changes slowly, and is led by firms with strong marketing resources (e.g., P&G, Sara Lee). These aspects of differentiation improve the generalizability of the results.

⁹ There are 18, 5 and 21 four digit codes respectively for Foods, Personal Care and Electronics industries.

4.3. Data and Sample Collection Procedure

The stocks of both acquirer and target firms are listed and traded on one of the four major U.S. exchanges (i.e., NYSE, AMEX, NASDAQ, and OTC). A sample of M&A agreements announced during this period was collected from the Securities Data Corporation (SDC) Thompson Mergers and Acquisitions database. It provides full histories, including announcement dates and other material terms and conditions of the deal. In order to verify the announcement dates provided by SDC, I also independently consulted various published sources such as wire service reports (*PR Newswire/Rueters*), *Wall Street Journal* and other magazines for information regarding the merger. In approximately 20% of cases, these did not match the SDC date, and I used the verified announcement dates as the event dates. To ensure that there is no leakage of information regarding the merger, I searched the published sources for any news item pertaining to *both* the target and acquirer firm together. In those cases where there was preliminary information concerning a potential merger, the deal was deleted from the sample. Approximately 10% of the deals I originally identified were deleted because of leakage concerns.¹⁰ To identify reliable and meaningful data, several restrictions were placed on the sample. First, both the acquiring and the target firms had to be publicly traded. Otherwise, it was not possible to get financial market data. Second, data for the acquirer and target firms had to be available in both the daily return tape of the Center for Research in Security Prices (CRSP) and the COMPUSTAT datasets to allow me to obtain the required stock market information and accounting information respectively. Finally, when acquirers were involved in multiple acquisition announcements in a year, I only

¹⁰ Where the leakage involved actual information concerning the merger (2% of the original cases), I retained the merger for further analysis, using the earliest date of merger announcement as my event date.

considered the first one in order to avoid confounding the effects of two separate mergers. The approach generated a final sample size of 97 for the Electronics industry and 102 for the FPC. Table 1 provides an overview of the data, sources and the measures.

[Insert Table 1 about here]

4.4. Measures

4.4.1 Dependent Variables I used financial market data for both dependent variables. The daily return file of CRSP provides the stock return data to calculate the cumulative abnormal returns, which is subsequently used to calculate the wealth gains accruing to the target and acquirer separately (see Appendix A for details). Synergistic gains are operationalized as the weighted average of the wealth gains accruing to the acquirer and target firm. The equity market value of the firm is calculated by multiplying the total share outstanding and the price of the stock, both of which were obtained from CRSP.

4.4.2 Independent Variables *Strategic Emphasis.* Following Mizik and Jacobson (2003), my view of strategic emphasis examines the relative emphasis that a firm places on building brand or R&D resources. I operationalize strategic emphasis by subtracting the R&D investment from the advertising spending and dividing it by the total assets of the firm in the year preceding the merger. Measures of advertising, R&D and total assets were obtained from COMPUSTAT. Similarity in strategic emphasis refers to the context where both the firms have same strategic emphasis (both marketing or both R&D). Under the complementarity in the strategic emphasis, merging firms have different strategic emphasis.

Consolidation versus Diversification. Traditional measures of diversification rely on SIC codes to assess the extent of the firm's operations in different industries (Pitts and

Hopkins 1982). From the COMPUSTAT industrial data file, I obtained revenues for each of the different segments within which the firm operates. When the dominating (highest revenue) segments of the merging firms have identical four-digit SIC codes, I consider the transaction to be consolidation-based; otherwise it is considered as diversification-based.¹¹

Control Variables. The R&D resources and the brand resources of the target and acquiring firms are also included as control variables. Brand resources are operationalized as total expenditures in advertising, and R&D resources are operationalized as total expenditures in R&D, both drawn from COMPUSTAT. Furthermore, *relative size* is included as a control because it has been found to impact M&A performance (e.g., Haspeslath and Jemison 1991). For example, when the acquirer firm is much larger than the target firm, necessary critical mass is absent. As a result, the integration process is problematic and the combination potential of the merger is often unrealized (Kusewitt 1985). The relative size of the firms is calculated as the ratio of target sales and acquirer sales (e.g., Capron 1999; Seth 1990b) for the year preceding the acquisition.¹² Sales data were obtained from COMPUSTAT.

4.5. Approach to Analysis: Model Specification and Estimation

I use ordinary least squares to test the hypothesized relationships. Prior to constructing the interactions, I mean-centered the relevant continuous predictors to

¹¹ CRSP also assigns SIC code to describe a firm's business. Kahle and Walkling (1996) compare sample matched on COMPUSTAT and CRSP SIC codes and conclude that the use of SIC codes assigned by COMPUSTAT are more powerful in detecting abnormal performance.

¹² I also considered using ratio of employees (e.g., Rust, Moorman, and Dickson 2002), but found that the correlation between the sales and employee-based ratios is very high (> .90). The regression results also do not change materially when one measure is used in place of the other.

reduce any potential multicollinearity between the main and interaction effect (Aiken and West 1991). An examination of variance inflation factors for all coefficients suggested that multicollinearity was not a serious problem in any of the models (Gujarati 1995). Also, I examine the standardized coefficients to facilitate interpretation of the results. As I previously mentioned, firm performance is assessed through synergistic gains and acquirer wealth. Each of these is being used, in turn, as the dependent variable in the estimated equations. The models take the following form.

Model 1

$$Y = \beta_0 + \beta_1(\text{Acquirer Brand Resources}) + \beta_2(\text{Acquirer R\&D Resources}) + \beta_3(\text{Relative size}) + \beta_4(\text{Acquirer Strategic Emphasis}) + \beta_5(\text{Target Strategic Emphasis}) + \varepsilon$$

Model 2

$$Y = \beta_0 + \beta_1(\text{Acquirer Brand Resources}) + \beta_2(\text{Acquirer R\&D Resources}) + \beta_3(\text{Relative size}) + \beta_4(\text{Acquirer Strategic Emphasis}) + \beta_5(\text{Target Strategic Emphasis}) + \beta_6(\text{Acquirer Strategic Emphasis} \times \text{Target Strategic Emphasis}) + \varepsilon$$

Model 3

$$Y = \beta_0 + \beta_1(\text{Acquirer Brand Resources}) + \beta_2(\text{Acquirer R\&D Resources}) + \beta_3(\text{Relative size}) + \beta_4(\text{Acquirer Strategic Emphasis}) + \beta_5(\text{Target Strategic Emphasis}) + \beta_6(\text{Acquirer Strategic Emphasis} \times \text{Target Strategic Emphasis}) + \beta_7(\text{Motive}) + \varepsilon$$

Model 4

$$Y = \beta_0 + \beta_1(\text{Acquirer Brand Resources}) + \beta_2(\text{Acquirer R\&D Resources}) + \beta_3(\text{Relative size}) + \beta_4(\text{Acquirer Strategic Emphasis}) + \beta_5(\text{Target Strategic Emphasis}) + \beta_6(\text{Acquirer Strategic Emphasis} \times \text{Target Strategic Emphasis}) + \beta_7(\text{Motive}) + \beta_8(\text{Acquirer Strategic Emphasis} \times \text{Motive}) + \beta_9(\text{Target Strategic Emphasis} \times \text{Motive}) + \beta_{10}(\text{Acquirer Strategic Emphasis} \times \text{Target Strategic Emphasis} \times \text{Motive}) + \varepsilon$$

Model 1 represents a baseline model that tests the effect of the control variables. It includes two acquirer resources and the main effects of the acquiring and target firms' strategic emphases. The hypotheses testing portion of the analysis is initiated through Model 2. It adds to Model 1 an interaction term between acquirer strategic emphasis and target strategic emphasis. Model 3 adds merger motive¹³ to Model 2. Finally, Model 4

¹³ Motive is a dummy variable, where consolidation=1, and diversification =0.

introduces the three way interactions among acquirer strategic emphasis, target strategic emphasis and motive. Irwin and McClelland (2001) recommend that all lower order interactions be included in a model in order to properly interpret higher order interaction effects. Accordingly, I add all two and three-way interactions between the strategic emphasis and motive variables to Model 3. A comparison of Model 2 to Model 1 tests H_1 , Model 3 versus Model 2 tests H_2 , and Model 4 versus Model 3 tests H_3

5. CHAPTER FIVE: RESULTS

5.1. Descriptive Statistics

The means, standard deviations, and correlations for the research variables are shown in Table 2 and Table 3. The descriptive statistics reveals some variability in the measures of the major constructs across two industries. Average strategic emphasis values of the constituents firms are negative in Electronics and positive in FPC. It indicates that R&D is the dominant strategic emphasis in Electronics, while in FPC, marketing strategic emphasis assumes more importance. Also, brand resources of the acquirer are negatively correlated with synergistic gains in Electronics, while the same relationship is positive in FPC.

[Insert Table 2 and 3 here]

Figure 2 -7 illustrate the cumulative abnormal returns accruing separately to the target and acquirer firms for both industries. It can be seen that cumulative abnormal returns to target firms are primarily positive (Electronics: $M = .15$, $SD = .27$; FPC: $M = .17$, $SD = .23$), whereas the cumulative abnormal returns to acquirer firms are on average zero (Electronics: $M = .00$, $SD = .09$; FPC: $M = .00$, $SD = .07$). The overall synergistic gains are positive for both industries (Electronics: $M = 52.03$, $SD = 491.82$; FPC: $M = 76.60$, $SD =$

620.28). The asymmetric distribution between acquirer and target is in accordance with past research in finance and strategy (e.g., Bruner 2002; Datta, Pinches, and Narayanan 1992; Jensen and Ruback 1983). These descriptive statistics also indicate that my sample drawn from different industries shares a similar profile with larger, multi-industry samples and thus provide some support for the external validity of the results.

5.2. Test of Hypotheses

The estimation results of the multiple regressions are shown in Tables 4 and 5. The results are presented separately for the Electronics industry (see Table 4) and FPC (see Table 5) which I discuss subsequently. For both the dependent variables, I ran Model 1-4 as described previously. Model 1 includes only the control variables. As is evident in Table 4, the overall Model 1 is significant in the Electronics industry across both dependent variables (synergistic gains: $F_{(5,91)} = 3.43, p < .01$; acquirer wealth: $F_{(5,91)} = 4.26, p < .01$). Model 1, however, is not significant for FPC for any of the dependent variables (synergistic gains: $F_{(5,96)} = 1.87, ns$; acquirer wealth: $F_{(5,96)} = 1.83, ns$). Model 4 – the most comprehensive model I test – explains roughly a third and a fourth of the overall variance in the two dependent variables for Electronics and FPC respectively. Table 4 and 5 also report F-test values for comparisons between models. In each case, the F-test assesses whether or not the more complex model represents a statistically significant improvement over the simpler model to its immediate left in the table. The change-in-F associated with the inclusion of variables along with the significance level of the variable provides a test of my hypotheses. The general pattern of results for both synergistic gains and acquirer wealth is the same. Further, I submit these results to an additional test to examine the three-way interaction in more depth utilizing the

procedures recommended by Aiken and West (1991), Irwin and McClelland (2001) and Jaccard, Turrisi, and Wan (1990).

[Insert Table 4 and 5 here]

5.2.1 Electronics Industry Results My first hypothesis investigates whether similarity or complementarity in strategic emphasis yield positive market response. In testing this hypothesis, I include acquirer strategic emphasis, target strategic emphasis and the interaction of these two in Model 2 and compare it with Model 1. As can be seen, the overall Model 2 is significant for both the dependent variables. (synergistic gains: Model $F_{(6, 90)} = 4.55, p < .01$; acquirer wealth: Model $F_{(6, 90)} = 5.07, p < .01$). Further, the inclusion of the acquirer and target strategic emphasis and their interaction results in a significant improvement in model fit over comparable Model 1 without these variables (synergistic gains: $\text{change-in-}F_{(1,90)} = 8.69, p < .01$; acquirer wealth: $\text{change-in-}F_{(1,91)} = 7.28, p < .01$;). Looking at the Model 2, the interaction between the acquirer and the target strategic emphasis is positive and significant for both dependent measures (synergistic gains: $b = .27, p < .01$; acquirer wealth: $b = .25, p < .01$). The positive sign on the interaction coefficient suggests that similarity (not complementarity) is positively associated with both my dependent variables. Thus, I find support for hypothesis H_{1a} .

H_2 has to do with the role of merger motive. For synergistic gains, the addition of the motive leads to a significant improvement in model fit in the case of Model 3 relative to Model 2 ($\text{change-in-}F_{(1, 89)} = 4.68, p < .01$) The overall Model 3 is also significant (Model $F_{(7,89)} = 4.73, p < .01$). Looking at the results in Model 3, the main effect yields a positive and significant coefficient for this variable ($b = .20, p < .01$), suggesting that the consolidation motive produces higher gains in a merger than a diversification motive.

This result is in line with what I predicted about synergistic gains in hypothesis H₂. However, I do not find evidence to support the hypothesis for acquirer wealth. As can be seen, Model 3 does not add significantly to Model 2 (change-in-F_(1, 89) = 1.23, *ns*) and the coefficient for motive is not significantly different from zero (*b* = .14; *ns*). Thus H₂ is not supported for acquirer wealth creation.

H₃ suggests that under consolidation merger motive, similarity in strategic emphasis would be more conducive to synergistic gains. To model this, I included the interactions of merger motive and the target and acquirer strategic emphasis in Model 4. For both the dependent variables, the change-in-F are significant relative to Model 3 which did not include these variables (synergistic gains: change-in F_(3,87) = 2.96, *p* < .01; acquirer wealth: change-in F_(3,87) = 3.07, *p* < .01). The overall Model 4 is also significant across both the dependent variables (synergistic gains: Model F_(3, 86) = 2.93, *p* < .05; acquirer wealth: F_(3, 86) = 4.40, *p* < .01). Looking at Model 4, it appears that the three-way interaction of motive and acquirer and target strategic emphasis is positive and significant for both synergistic gains (*b* = .36, *p* < .05) and acquirer wealth (*b* = .33, *p* < .05). The results indicate that the positive impact of consolidation motive is strengthened in the presence of similarity in strategic emphasis alignment between the target and the acquirer. This is in line with what I predicted in hypothesis H₃.

5.2.2 FPC Industry Results¹⁴. Similar to the Electronics industry, I test the hypotheses via a series of models. As can be seen, for both synergistic gains (Model F_(6, 96) = 2.33, *p* < .05) and acquirer wealth (F_(6, 96) = 2.98, *p* < .05), the overall Model 2 is significant. Further, for both the dependent variables, the inclusion of the acquirer and target strategic

¹⁴ As I have data for a 21 year period, I controlled for the period. None of the year dummies was significant and to conserve the degrees of freedom, I did not include those in the final model.

emphasis and their interaction results in a significant improvement in model fit over a comparable Model 1 without these variables (synergistic gains: change-in-F_(1,95) = 4.41; $p < .01$ and acquirer wealth: change-in-F_(1,95) = 6.77; $p < .05$). Model 2 also indicates that interaction between the acquirer and the target strategic emphasis is positive and significant for both the dependent variables ($b = .21, p < .05$; $b = .29, p < .01$). This result is consistent with the notion that similarity in strategic emphasis rather than complementarity is associated with value creation. Thus, I have consistent support for H_{1a} across two contexts.

H₂ pertains to the role of merger motive and I predicted a positive relationship between consolidation motive and value creation. For synergistic gains, the addition of the motive leads to a significant improvement in model fit in the case of Model 3 relative to Model 2 (change-in-F_(1, 94) = 3.39, $p < .01$). The overall Model 3 is also significant (Model F_(7, 94) = 2.55, $p < .05$). As evidenced in Model 3, the main effect of merger motive is marginally significant and positive predictor of synergistic gains ($b = .18, p < .10$), in support of H₂. Therefore, similar to the Electronics, hypothesis H₂ is also supported for synergistic gains. This result, however, is different for acquirer wealth. It can be seen that adding motive does not lead to any improvement in the Model 3 relative to Model 2 (change-in-F_(1, 94) = 1.13, *ns*) and the main effect of motive is also not significant ($b = .09, ns$). Therefore, H₂ is not supported for acquirer wealth.

In order to test the hypothesis H₃, the interactions of merger motive and the target and acquirer strategic emphasis are added in Model 4. The change-in-F is significant relative to Model 3 which did not include these variables (synergistic gains: change-in-F_(3, 91) = 3.68, $p < .01$ and acquirer wealth change-in-F_(3, 91) = 5.62, $p < .01$). Overall Model

4 is significant for both the dependent variables (synergistic gains: Model $F_{(10, 91)} = 2.85$, $p < .01$, $R^2 = .24$ and acquirer wealth Model $F_{(10, 91)} = 3.00$; $p < .01$, $R^2 = .25$). The three-way interaction of motive and acquirer and target strategic emphasis is marginally significant (at $p < .10$) for both the dependent variables. However, the estimated effect is in negative direction (synergistic gains: $b = -.24$, acquirer wealth: $b = -.22$). Therefore, contrary to the Electronics industry case, this implies that the positive impact of consolidation motive is *weakened* in the presence of high strategic emphasis alignment between the target and the acquirer. This result contradicts H_3 .

To further explore these three way interactions, I next present the post-hoc probing.

5.2.3 Post-Hoc Analysis To get a better feel for the phenomenon, I further illustrate the impact of the interaction between motive and strategic emphasis alignment. To do so, I examine the specific types of strategic emphasis for acquirers and targets and their impact on two dependent variables using the post-hoc probing procedures (Aiken and West 1991; Irwin and McClelland 2001; Jaccard, Turrisi, and Wan 1990). As Irwin and McClelland (2001) note, such post-hoc probing provides a deeper understanding of the interrelationships between different levels and combinations of the independent variables on the dependent variable. Accordingly, I use the original continuous measures of strategic emphasis to best understand the richness of this interaction.

Because I have measures for both acquirer and target strategic emphasis, I repeated this post-hoc analysis using the acquirer and target strategic emphases in turn as a starting point. To simplify the explication here, I describe in detail only the effects on synergistic gains that result for changing levels of target strategic emphasis. This is

presented in Table 6. The intuition is similar when acquirer strategic emphasis is used as the starting point.

[Insert Table 6 here]

The probing involves multiple steps (Aiken and West 1991, pp. 56-58). First, I created a high level of target strategic emphasis, set at one standard deviation above the mean-centered main effect. Using this high level of target strategic emphasis, I re-estimated the model and examined the significance of the interactions. Results indicate whether the interaction between target strategic emphasis and motive is significant for a high level of acquirer strategic emphasis. This resulting parameter is significant and positive for the Electronics ($\beta = .85, p < .01$), but significant and negative for the FPC industry ($\beta = -.54, p < .05$).

Next, I examine the effect of changing levels of the motive. Given that the target strategic emphasis is high, I created a high level of motive one standard deviation above the mean-centered main effect and re-estimated the model. This approach allowed me to examine, for a consolidation motive, whether the acquirer's strategic emphasis improves performance, when the target strategic emphasis is already high. Therefore, I focus here on target strategic emphasis. The results indicate that acquirer strategic emphasis is positive and significant for the Electronics industry ($\beta = .88, p < .01$). The parameter for FPC industry is insignificant ($\beta = .10, ns$). This means that for a firm with a consolidation motive, the acquirer's marketing strategic emphasis has a positive effect on performance when target also has a marketing strategic emphasis in the Electronics industry.

I completed my post-hoc probing by examining the effect of the acquirer's strategic emphasis when the target has a marketing strategic emphasis and the merger

motive is diversification. This allows me to examine whether, for a diversification merger, increasing levels of the target's marketing emphasis hurts synergistic gains when acquirer also has a marketing emphasis. To examine this, I constructed a diversification motive, by deducting one standard deviation from the mean-centered main effect) and re-estimated the model. Results (as seen in Table 6) indicate that the acquirer's strategic emphasis is now negative and significant for the Electronics ($\beta = -.41, p < .01$) but remains positive and significant for FPC ($\beta = .59, p < .01$). It indicates that in Electronics industry, when a firm has a diversification motive, and the acquirer has a marketing strategic emphasis, increasing the target's marketing strategic emphasis also exerts a negative impact on synergistic gains. However, this is not true for the FPC.

[Insert Figures 8-15 here]

These results are further illustrated in Figure 8 through Figure 15 for both industries. In Figure 8, the synergistic gains under the consolidation motive for various combinations of acquirer and target strategic emphasis are depicted for the Electronics. As can be seen, when the acquirer and target both have marketing strategic emphases the synergistic gains are positive ($M_{\text{acquirer marketing and target marketing}}=1485$) and when both the acquirer and target have an R&D strategic emphasis, the synergistic gains are also positive ($M_{\text{acquirer R\&D and target R\&D}}=1589$). However, when the acquirer and target have varying strategic emphases, the synergistic gains are negative ($M_{\text{acquirer marketing and target R\&D}}=-313$; $M_{\text{acquirer R\&D and target marketing}}=-257$). Figure 10 demonstrates the identical pattern for acquirer wealth.

Next, I examine the results pertaining to FPC industry under consolidation motive. The results are different from Electronics for both synergistic gains and acquirer

wealth as indicated in Figure 12 and 14 respectively. When both the firms have strategic emphasis in marketing under consolidation motive, both synergistic gains ($M_{\text{acquirer marketing and target marketing}}=-670$) and acquirer wealth ($M_{\text{acquirer marketing and target marketing}}=-781$) are negative. However, I find expected results for the other similarity condition, as both synergistic gains ($M_{\text{acquirer R\&D and target R\&D}}=880$) and acquirer wealth are positive ($M_{\text{acquirer R\&D and target R\&D}}=581$) when both firms have strategic emphasis in R&D. Synergistic gains are also different under two different complementarity conditions. As expected, synergistic gains and acquirer wealth are negative when acquirer has R&D emphasis and target has marketing emphasis (synergistic gains: $M_{\text{acquirer R\&D and target marketing}}=-241$, acquirer wealth $M_{\text{acquirer R\&D and target marketing}}=-379$). However, the other complementarity condition yields positive effect on both synergistic gains ($M_{\text{acquirer marketing and target marketing}}=1496$) and acquirer wealth ($M_{\text{acquirer marketing and target marketing}}=1128$).

For the diversification motive, the results are exactly opposite for Electronics. As can be seen in Figure 9, when the acquirer and target have differing strategic emphases, the synergistic gains are positive and significant (e.g., $M_{\text{acquirer marketing and target R\&D}}=227$; $M_{\text{acquirer R\&D and target marketing}}=18$). In contrast, when the acquirer and target have similar strategic emphases, the synergistic gains are both negative ($M_{\text{acquirer marketing and target marketing}}=-1738$; $M_{\text{acquirer R\&D and target R\&D}}=-1791$). Figure 11 indicates identical pattern for acquirer wealth. This is in accordance with my prediction.

Figure 13 and 15 shows the synergistic gains and acquirer wealth under the diversification motive for various combinations of acquirer and target in FPC. As can be seen, synergistic gains and acquirer wealth are positive and significant for one complementarity condition and negative for the other. Specifically, when acquirer has

marketing strategic emphasis and target has R&D strategic emphasis, the synergistic gains are positive ($M_{\text{acquirer marketing and target R\&D}}=774$). From Figure 15, acquirer wealth is also positive under the same condition ($M_{\text{acquirer marketing and target R\&D}}=209$). However, both synergistic gains and acquirer wealth are negative when acquirer strategic emphasis is R&D and target strategic emphasis is marketing (synergistic gains: $M_{\text{acquirer R\&D and target marketing}}=-227$; acquirer wealth: $M_{\text{acquirer R\&D and target marketing}}=-174$). Next, I turn to the similarity condition. As expected, synergistic gains and acquirer wealth are negative when both the firm have strategic emphasis in R&D (synergistic gains: $M_{\text{acquirer R\&D and target R\&D}}=-47$, acquirer wealth: $M_{\text{acquirer R\&D and target R\&D}}=-575$). However, the result is different under the other similarity condition. As can be seen, synergistic gains are positive when both the firms have strategic emphasis in marketing ($M_{\text{acquirer marketing and target marketing}}=495$). The same combination also yields positive acquirer wealth ($M_{\text{acquirer marketing and target marketing}}=383$).¹⁵

Two types of similarity can exist as both firms in a merger have either marketing emphasis or R&D emphasis. There can also be two forms of complementarity: acquirer has strategic emphasis in marketing and target has strategic emphasis in R&D and vice versa. The nature of the primary industry within which the acquiring firm operates affects

¹⁵The analyses thus far assume that when the target and acquirer firm have the same 4-digit SIC codes, the merger is consolidation-based. All other mergers are viewed as diversification-based. An alternative approach to operationalizing merger motive is to use the degree of similarity between the acquirer and target firms' industries. I re-operationalized the motive variable to capture the degree of similarity between the firms using the 4-digit SIC codes. When the target and acquirer had the same 4-digit SIC code, the motive variable was given a value of 4. When only the first 3-digits of the 4-digit SIC code overlapped, the motive variable was given a value of 3. Similarly, when the first two digits overlapped, the motive variable was set at a value of 2. Finally, when only the first digit overlapped, the motive variable had a value of 1. When no overlap existed, the motive variable had a value of zero. I re-ran all of my analyses using this finer-grained measure of motive. Interestingly, these latter results were essentially identical to my earlier findings. Due to the relative ease of interpretation associated with using a dummy variable, and because this represents a more conservative way of measuring the consolidation motive, I describe only the original results in detail here.

the value of its resources, and also affects the type of resources it seeks through merger. Typically, firms will seek to acquire and control those resources that are most valuable for maintaining a competitively superior position (Barney 1991; Hunt and Morgan 1995).

In Electronics industry, high rate of technological turbulence is likely to favor firms that have strong focus in R&D. The leading firms are most likely to have strategic emphasis in R&D so that they have a deeper understanding of new technologies and innovations. Also, firms operating in this industry will seek target for accessing diverse knowledge bases and integrating different technologies. In this industry characterized by rapid technological changes, greater technological diversity will allow firms to explore new technologies and keep abreast of the latest technological advancements. In the FPC industry, the relatively slow pace of change and high degree of market predictability leads firms to look for resources that can be of help in reducing cost of production, marketing, and delivery. Leading firms are most likely to have a strong *marketing* strategic emphasis and they are the most likely to be able to integrate resources acquired from the target firm into their existing resource chains to improve overall performance. In contrast, firms with a strong R&D emphasis are likely to have weaker competitive positions that they cannot easily overcome through acquisition, given the stable nature of the industry. This suggests that the type of strategic emphasis and the degree of alignment both should be considered in examining value creation in stable and turbulent industry contexts.

In the Electronics industry, given the technology intensive nature of market, acquirers are likely to seek target firms that provide them with unique knowledge bases and superior strategic options for the future. This leads both marketing- and R&D-

focused firms to prefer targets that have strategic emphasis in R&D. Taken together, these predictions suggest that post-merger success will be highest when two R&D strategic emphasis firms combine in an Electronics industry context.

The expected effects are different in the FPC industry. Although similarity or complementarity in strategic emphasis will have an identical impact like Electronics, the RBV makes different predictions for the FPC than Electronics industry. If similarity holds, then post-merger performance will be highest when two firms with a marketing emphasis are brought together, whereas below average performance will result when an R&D focused firm acquires a marketing-focused firm. Under the complementary logic, the best performance will be under the condition when marketing emphasis of acquirer and R&D emphasis of target merge.

How do these effects vary based on motive? I hypothesized that in a consolidation setting, similar strategic alignments will be capable of generating greater value (compare to diversification setting). I find strong support for this in the context of Electronics industry (See Figure 8). But there is only partial support in the FPC context. There is a positive impact on value creation when both the firms have strategic emphasis in R&D. However, this relationship is reverse with the other form of similarity, i.e., when both firms have marketing strategic emphasis. Another notable finding is the strong positive impact of a particular complementarity condition. The result indicates (Figure 10) that there will be a positive value creation when acquirers with marketing strategic emphasis merge with firms strong in R&D.

Under diversification motive, I expected complementarity of strategic emphasis between the firms to play a positive role in value creation. Once again, it was supported

in the context of Electronics industry. Further, as expected, the combination of acquirer marketing and target R&D strategic emphasis proved to be better than the acquirer R&D and target R&D combinations. The result is different in FPC. I find strong support for the combination of acquirer marketing and target R&D; however, the other combination of complementarity is negatively related with value creation. Therefore, the expected superiority of complementary strategic emphasis combinations is supportive only in the context of Electronics industry.

5.3. Additional Analysis

In order to investigate these results further, I examined accounting-based cost measures collected two years after the completion of the mergers within my sample, and compared them to pre-merger values. I expect that similarity in strategic emphasis between the firms to lead to greater ease of integration, reduced friction and greater economies of scale, all of which could be expected to result in post-merger cost-savings.

The assessment of acquiring firm's operating performance using accounting data has produced mixed results. Much of the previous work has shown that acquiring firm's accounting rate of returns and profitability after the acquisitions either deteriorate or show little improvement (e.g., Fowler and Schmidt 1988; Ravenscraft and Scherer 1987). Other studies, however, report improved operating performance (Healy, Palepu, and Ruback 1992; Cornett and Tehranian 1992). Healy, Palepu, and Ruback (1997), however, report in a subsequent study that the return will depend on whether the premium paid to target is taken into account or not.

Consistent with past research (Fee and Thomas 2004), I focus on the change in selling and general administrative expenses (SGA) to sales ratio as a measure of cost

efficiency. To determine the cost savings achieved through merger, I first calculate this ratio separately for the two merging firms one year prior to the merger completion date. I then weight these ratios according to the individual firms' sales in that year. Second, I calculate the same ratios for one year following the completion of the merger. I then subtract the post-merger weighted ratio from the pre-merger weighted ratio. If the merger successfully produced cost efficiencies, the change in cost (selling, general and administrative expenses to sales) ratio should be negative. On average, the mergers in my sample achieved a modest improvement in cost-efficiency for Electronics ($M=-.044$, $SD=.22$; $p < .05$). The effect was insignificant for FPC ($M=-.008$ $SD=.07$; ns).

For the Electronics, I further examine how these savings can vary based on the strategic emphases of the target and acquirer, their interaction and the merger motive. In order to do this, I separately regressed the savings ratio against the predictor variables described for Model 4. The regression results are presented in Table 7.¹⁶ Examining the impact of acquirer and target strategic emphasis on cost efficiencies, the three way interaction between motive, acquirer strategic emphasis, and target strategic emphasis is significant and negative ($\beta=-.55$; $p < .01$), a finding that is consistent with my earlier analysis and with hypothesis H₃. To better understand these results, I again used the post-hoc probing methods recommended by Aiken and West (1991).

¹⁶ Of the 97 transactions in the original Electronics sample, only 73 were available for the analysis of accounting data. I tried unsuccessfully to obtain the accounting data for the missing observations from other sources including *Factiva* and *Mergents Online*. The 24 missing observations represent firms that were delisted from stock exchanges (17), firms which subsequently formed part of another merger (3), and firms which underwent a name change/liquidation (4). I also compared the firm sizes for the 24 lost observations and the 73 retained values. In addition, I compared the synergistic gains of the retained sample with those of the missing observations. T-tests indicate that the retained sample is comparable to the missing observations in terms of the synergistic gains following the merger announcement ($M_{\text{dropped}}= 71$; $SD = 373$; $M_{\text{retained}}=49$; $SD = 523$; $t\text{-value} = .22$; ns). Therefore, I am confident that the lost observations do not in any way result bias the results of the current analysis.

[Insert Figure 16 and 17 here]

Figure 16 and 17 present the cost efficiencies for the various conditions. The pattern of cost efficiencies across the various conditions is remarkably consistent with the synergistic gains results reported previously. Cost efficiencies are significant under the consolidation motive when both acquirer and target have similar strategic emphases ($M_{\text{acquirer marketing and target marketing}} = -.34$; $M_{\text{acquirer R\&D and target R\&D}} = -.64$). However, when the target and acquirer strategic emphases are different, the costs post-merger actually increase ($M_{\text{acquirer marketing and target R\&D}} = .17$; $M_{\text{acquirer R\&D and target marketing}} = .01$). This pattern is reversed when I examine the cost efficiencies under diversification motive. In this case, when the target and acquirer have differing strategic emphases, the post-merger costs decline ($M_{\text{acquirer marketing and target R\&D}} = -.15$; $M_{\text{acquirer R\&D and target marketing}} = -.26$). In contrast, when the target and acquirer have similar strategic emphases and the merger is diversification-based, costs increase significantly ($M_{\text{acquirer marketing and target marketing}} = .19$; $M_{\text{acquirer R\&D and target R\&D}} = .22$). Thus, overall the results of the accounting data substantiate and extend what was observed in the stock market analysis. A high degree of strategic emphasis alignment in a consolidation-based merger context produces greater cost savings following merger completion.

6. CHAPTER SIX: SUMMARY AND CONCLUSIONS

6.1. General Discussion

An accumulating body of research could not shed light on the determinants of M&A successes and failures. In a recent article providing an assessment of M&A performance spanning a 74-year period of scholarship, King et al. (2004, p. 197) point out that “researchers may not be looking at the right set of variables as predictors of post

acquisition performance.” In an attempt to gain richer insights into this phenomenon, I present a new focus of inquiry and explain variance in M&A performance through the resource configuration of merging firms. My findings represent a step forward in explaining the previously puzzling observation about M&A performance. Collectively, these results demonstrate interesting patterns of significant relationships among strategic emphasis alignment, merger motives, and M&A performance.

Although past research has examined the relative impact of marketing versus R&D resources (Mizik and Jacobson 2003), this study is the first to demonstrate that the nature of strategic emphasis alignment between a target and an acquirer plays a crucial role in value creation from a merger. The choice of strategic emphasis (marketing versus R&D) involves tradeoffs and defines the manner in which a firm chooses to compete (Porter 1996). Across firms, the *relative* emphasis on value creation through innovation (R&D competencies) versus value appropriation (marketing competencies) typically varies, even within a single industry. The relative role of marketing or R&D within a firm at any given point in time defines its strategic emphasis, and as such provides information to the stock market regarding the firm’s strategic priorities. I demonstrate that the relative emphasis on marketing resources provides a strong signal to the stock market under certain types of mergers. In doing so, I respond to the call for more research linking marketing actions and resources with financial performance (*Marketing Science Institute, 2004-2006 Research Priorities*).

This research also contributes to the theories of resource relatedness and helps resolve the debate in the literature concerning the value of resource similarity and resource complementarity (Harrison et al. 1991, 2001; Hoskisson and Busnit 2002). I find

considerable support that similarity, rather than complementarity, in the strategic emphasis alignment between the merging firms leads to positive M&A performance. This finding is robust across the two industries that I studied. These two industries are different from each other in significant ways and this establishes the convergent validity of the results. As firms with similar strategic emphases share similar priorities, they are more likely to minimize culture clashes that have been shown to undermine the success of mergers. For instance, Epstein (2004) suggests that one key element of post-merger success in the case of the JPMorganChase merger was articulating and defining a post-merger business model that was acceptable to various stakeholders. A high degree of strategic emphasis alignment enhances the ability of the combined entity to set priorities, and facilitates post-merger integration between the firms. This is in line with prior research that suggests that similarity between the acquirer and target will help the acquirer gain and absorb knowledge from the target.

Larsson and Finkelstein (1999) demonstrated that both resource complementarity and resource similarity can lead to synergy realization in a merger context, but did not provide a framework that shows when each is likely to be more valuable. The results demonstrate that merger motive plays a critical role in determining whether resource similarity (in the case of consolidation) or resource complementarity (diversification) will enhance firm value in the long run. Specifically, when the strategic emphasis alignment between a target and acquirer in a merger is high, superior post-merger gains will result, particularly when the merger is consolidation-based.

Other benefit of high strategic emphasis alignment is the potential to gain cost efficiencies arising from economies of scale. Particularly when the merger is

consolidation-based, economies of scale (i.e. operational synergies) arising from pooling marketing or R&D resources are likely to generate significant cost savings. While prior research has generally focused on the role of consolidation-based (or related mergers) versus diversification-based mergers, findings have generally been mixed (e.g., Anand and Singh 1997; Chatterjee 1986; Lubatkin 1983; Seth 1990a; Singh and Montgomery 1987). My research suggests that consolidation-based mergers are valued more highly by the market, but this effect is moderated by the resource configurations of the target and acquirer firms.

6.2. Implications for Theory Development

Research suggests that M&A can be a way for firms to manage their resource profiles (Ahuja and Katila 2001; Capron and Pistre 2002) and to overcome problems in the exchange of resources (e.g., Anand and Delios 2002). My primary contribution illustrating the value of understanding the underlying, complex relationship between an acquiring firm's resources and those of the target firm offers important insights for future theoretical development.

First, this research contributes a model of resource configuration that builds on our understanding of M&A performance. M&A has been an important strategic choice for firms to leverage resources and this phenomenon is germane to marketing strategy research and practice. Marketing scholars have called for more research on these issues (Capon and Glazer 1987; Wind and Mahajan 1997). And yet, a few empirical studies withstanding (Capron and Hulland 1999; Homburg and Bucerious 2005; Prabhu, Chandy, and Ellis 2005; Rao, Mahajan, and Varaiya 1991), the issue has received only limited attention from marketing scholars. Using RBV as a frame of reference, this research

adopts a marketing perspective and empirically substantiates the role of firm-specific resources on M&A performance.

Second, I respond to multiple calls that marketing needs to extend its focus from tactical to strategic considerations, and aggressively address corporate-level research issues (e.g., Day and Montgomery 1999; Kerin 1992; Varadarajan and Clark 1994). For example, Day and Montgomery (1999, p.11) caution that the marketing domain will be marginalized should marketers not address and contribute in management of these inter-functional issues. This study significantly enhances the understanding of marketing phenomena in the strategic decisions traditionally considered outside the marketing domain. M&A are important events and the study provides an appropriate “big picture” context to assess marketing productivity and highlight marketing’s functional prominence in the strategic dialogue of the firm. Such broadened perspectives significantly enhance the understanding of marketing phenomena in M&A context.

Third, I advance the field’s understanding about the issue of related versus unrelated acquisitions. I suggest that it is contingent on the resource configurations of the acquirer and target firms. Prior research has highlighted strategic fit between merging firms as an important contributor to merger performance (Chatterjee 1986; Lubatkin 1983, 1987; Salter and Weinhold 1979; Shelton 1988; Singh and Montgomery 1987). Much prior work examines strategic fit from the perspective of the degree of similarity between the industries of the target and acquirer firm. The results have been rather mixed. For instance, Lubatkin (1983) suggests that related acquisitions should outperform unrelated acquisitions. However, Chatterjee (1986) finds that unrelated acquisitions are actually more value-creating than related acquisitions. When the target and acquirer are

unrelated to each other based on industry membership, a complementary strategic emphasis enhances performance. In contrast, when target and acquirer belong to related industries, similarity in strategic emphasis enhances performance. Why? I speculate that when acquirer and target belong to related industries, the ability to integrate will be easier if they share similar norms and organizational culture. When both firms are strongly marketing-driven, they are able to combine their strengths more effectively and with less friction and generate greater economies of scale. Likewise, when both firms are strongly R&D-driven, again, their ability to generate economies of scale in related industries is greater. However, when the combining firms belong to unrelated industries, the motive is one of diversification of risk. Therefore, the combining firms are not looking to integrate product lines or to generate greater economies of scale. In unrelated industries, it is likely that the basis for competing is different from the firms' core strengths. Therefore, having a complementary strategic emphasis is likely to enable the merging firm to compete better in an unrelated context. Furthermore, by acquiring a firm with a complementary strategic emphasis, the firm increases its strategic options by forming new strengths or core competencies. Such new competencies are likely to be more critical when firms are entering into diverse and unrelated industries.

6.3. Implications for Practice

A surge of M&A activities is reshaping the business world by realigning the competitions and creating new product market opportunities. Yet most of these transactions do not live up to prior expectations. This study illustrates that strategic fit between acquirer and target can have an important bearing on explaining some of the inconsistent findings concerning the potential synergy achievable in M&A. While my

research findings are exploratory and need to be confirmed by further research effort, some practical implications can be proposed.

A major finding of potential interest to managers is the dominant role of similarity in strategic emphasis between the merging firms in creating value for both acquirer and the combined transactions. I find that firms with strong marketing or R&D resources tend to integrate better with firms of similar strengths. Overall, the framework illuminates the conditions under which M&A will work and offers managers a normative guideline for target selection. In demonstrating that the diversification motive may work well under complementary strategic emphasis, I provide evidence that diversification can also be an effective mode of growth. Research previously undertaken has mainly focused on the main effect of the merger motive. At the same time, the finding also provides an important boundary condition regarding mergers taking place in the same industry. Specifically, I find some support that diversification will work under complementarity in strategic emphasis between the merging firms. At the same time, I also provide an important boundary condition for consolidation merger motives. As such, merging firms that have similar strategic emphases and operate within the same industry have a greater probability of being successful.

Second, this finding serves to highlight some support that one particular combination of complementarity may be value enhancing. As my findings show, in the FPC industry, the combination of an acquirer with marketing emphasis and target with R&D emphasis is likely to enhance M&A performance. This suggests that acquirers with strong marketing resources deploy the innovation potential of targets more effectively. For example, if a firm with strong marketing resources can acquire a firm with good

scientists, then the good product ideas of the acquirer can be better translated into meaningful products and thereby commercialized.

The final managerial prescription from this study is the strong negative impact of one particular complementarity combination. Specifically, my results indicate that a merger between an acquirer with R&D focus and the target with marketing focus may not be beneficial in the FPC industry. It reflects investors' skepticism about the likelihood that the merger with such strategic fit will be well integrated. This finding is robust irrespective of merger motive.

6.4. Limitations and Future Research

The results of this study should be viewed with certain limitations in mind. Also, there are many issues beyond the scope of this study, some of which also point to additional avenues for future investigation. As a first limitation, I note that my sample includes only public firms. Moreover, the study was confined to M&A taking place in Electronics, Food, and Personal Care industries. Additional studies in more industries will be needed to explore the generalizability of my conclusions and reveal further insights. In addition, a larger sample size may allow for alternative modeling approaches and more refined assessment of the impact of strategic emphasis alignment. Second, this study did not address some potentially important influences, like employee reactions (e.g., Schweiger and Walsh 1990) or customer reactions to M&A. That would be a departure from traditional studies that have focused primarily on internal organizational aspects as success factors of post-merger integration. A fruitful avenue for further research would be to consider customer perceptions following M&A, which would require customer-based data. Third, I have not looked into the nuances of managerial

decision-making involved with the implementation of M&A acquisitions. It has been observed that executives have not always been rational decision-makers and sometimes the decisions are artifacts of managerial overcommitment (Haunschild, David-Blake, and Fichman 1994) and shareholders' wealth (Salter and Weinhold 1979). Further research could examine such links. Fourth, I have not considered the time aspect of the integration. Previous studies have focused on both the positive and negative consequences of speed in the integration process (e.g., Buono and Bowditch 1989; Schweiger and Walsh 1990). The escalating momentum and the desire to complete a transaction quickly often lead to a premature solution (Jemison and Sitkin 1986). Research on change management has also viewed speed as a key construct affecting success in organizational change (e.g., Pettigrew, Woodman, and Cameron 2001). I encourage future researchers to explore whether a quick or slow approach could account for any significant difference in post-merger performance. And finally, I could not control the form of payment (i.e., stock versus cash). This can be an important driver of post-merger performance and there is empirical evidence suggesting that the form of payment affects post-merger return (Agarwal, Jaffe, and Mandelker 1992; Andrade, Mitchell, and Stafford 2001). According to "Hubris hypothesis" of takeover (Roll 1986), and "Winner's curse hypothesis" of takeover (Varaiya 1989), managers might pay a premium for a firm that the market has already correctly valued. For the majority of transactions; the price information is not publicly available. A survey method could be employed to obtain feedback from managers about the price paid.

6.5. Conclusions

This research highlights marketing perspectives to improve current knowledge of M&A activities and factors contributing to its success. I use finance based metrics to state marketing's contribution in the familiar language of cash flows (e.g., Day and Fahey 1988). The results provide theoretical confirmation that resource configuration of the merging firms affects M&A performance. M&A has been a dominant strategic choice for firms to leverage or obtain resources. Mitchell and Mulherin (1996, p.125) claim that "the takeover route is the fastest and least-cost method to alter industry structure." Annual value of M&A activities routinely exceed \$1 trillion (Sidel 2003). Firms use M&A to acquire critical marketing resources such as brands, distribution channels, and sales expertise. However, as often as not these attempts at resource acquisition subtract rather than add value. Is it possible to suggest a condition that drives M&A success? My effort underlies these issues. The key assertion demonstrated here is that the acquirers should be looking for firms with which they are strategically aligned (i.e., they provide similar resources), when consolidation is the primary motive, but should seek low strategic alignment (i.e., complementary resources) when diversification is the aim. Thus I provide a firm-specific explanation of performance difference, where most previous work has examined deal-specific variables to do the same.

Table 1 Operationalization and Sources of the Key Constructs

Construct	Measure	Data Source
<i>Independent Variable</i>		
Merger Information		SDC and Dow Jones Interactive
Brand Resources	Total firm advertising expenditures	COMPUSTAT Annual Industrial
R&D Resources	Total firm R&D expenditures	COMPUSTAT Annual Industrial
Strategic Emphasis ¹	(Advertising expenditures- R&D expenditures)/ Total assets	COMPUSTAT Annual Industrial
<i>Dependent Variable:</i>		
Synergistic Gains	(Market value of acquirer x Cumulative abnormal return + Market value of target x Cumulative abnormal return)	CRSP Daily Stock Return file
Acquirer Wealth	Market value of acquirer x Cumulative abnormal return	CRSP Daily Stock Return file
<i>Moderator:</i>		
Merger Motives	Matching of dominant SIC code Consolidation: Same Diversification: Different	COMPUSTAT Business Segment
<i>Control Variables:</i>		
Relative Size	Total sales of target/Total sales of acquirer	COMPUSTAT Annual Industrial

¹Positive and negative value will indicate marketing and R&D strategic emphasis respectively

Table 2 Descriptive Statistics and Correlation Matrix: Electronics (N = 97)

Variable	Mean	S.D.	1	2	3	4	5	6	7	8
1. Synergistic Gains	52.03	491.82								
2. Acquirer Wealth	-12.39	437.55	.91**							
3. Acquirer Brand Resources	48.89	244.55	-.33**	-.40**						
4. Target Brand Resources	6.53	26.98	-.04	-.03	.04					
5. Acquirer R&D Resources	213.53	631.44	-.23*	-.28	.58**	.03				
6. Target R&D Resources	45.25	197.55	.19	-.05	.13	.06	.10			
7. Acquirer Strategic Emphasis	-.04	.15	-.08	-.07	.02	.13	-.09	.04		
8. Target Strategic Emphasis	-.07	.18	-.15	-.11	-.07	.15	-.13	-.03	.10	
9. Relative Size	.41	.70	.11	.01	-.09	.42**	.16	.01	-.09	.10

* $p < .05$; ** $p < .01$; N represents the number of transactions

Notes: S.D. = standard deviation

Table 3 Descriptive Statistics and Correlation Matrix: FPC (N =102)

Variable	Mean	S.D.	1	2	3	4	5	6	7	8
1. Synergistic Gains	76.60	620.28								
2. Acquirer Wealth	-26.61	537.86	.84**							
3. Acquirer Brand Resources	282.26	611.87	.20*	.19*						
4. Target Brand Resources	74.25	190.09	-.13	-.12	.06					
5. Acquirer R&D Resources	100.74	254.38	.02	.01	.73**	.09				
6. Target R&D Resources	25.64	119.29	.01	-.02	-.04	.52**	-.01			
7. Acquirer Strategic Emphasis	.03	.05	.19	.16	.45**	.05	.07	-.01		
8. Target Strategic Emphasis	.05	.12	-.06	-.05	.17	.20*	.12	-.06	.16	
9. Relative Size	.23	.30	.06	.03	-.05	.22**	-.04	.24*	-.19	-.10

* $p < .05$; ** $p < .01$; N represents the number of transactions

Notes: S.D. = standard deviation

Table 4 Multiple Regression Results: Electronics

	Synergistic Gains				Acquirer Wealth			
	Model 1	Model 2	Model 3	Model 4	Model 1	Model 2	Model 3	Model 4
A. Acquirer Brand Resources	-.27** -2.33^b	-.26** -2.27	-.24** -2.17	-.24** -2.19	-.35** 2.97	-.33** -2.94	-.32** -2.85	-.30** -2.73
B. Acquirer R&D Resources	-.09 -.81	-.10 -.88	-.11 -1.03	-.10 -.90	-.10 -.86	-.11 -.93	-.11 -1.02	-.13 -1.13
C. Relative Size	.09 .98	.11 1.19	.09 .94	.09 .95	.01 .02	.02 .20	.01 .06	.01 .09
D. Acquirer Strategic Emphasis	-.08 -.87	-.11 -1.23	-.10 -1.04	-.02 -.25	-.06 -.61	-.09 -.94	-.07 -.81	.01 .12
E. Target Strategic Emphasis	-.18 -1.87	-.18* -2.02	-.18* -1.96	-.08 -.76	-.15 -1.52	-.15 -1.65	-.14 -1.59	-.05 -.54
F. Acquirer Strategic Emphasis x Target Strategic Emphasis		.27*** 2.95	.22** 2.40	-.01 -.07		.25** 2.75	.21** 2.33	-.01 -.06
G. Motive			.20** 2.16	.12 1.23			.14 1.52	.05 .59
H. Acquirer Strategic Emphasis x Motive				-.01 -.16				-.11 -.93
I. Target Strategic Emphasis x Motive				-.05 -.44				.01 .02
J. Motive x F				.36*** 2.75				.33** 2.56
F-value	3.43***	4.55***	4.73***	4.40***	4.26***	5.07***	4.74***	4.41***
Degrees of Freedom	(5, 91)	(6, 90)	(7, 89)	(10, 86)	(5, 91)	(6, 96)	(7, 89)	(10, 86)
Change in F		8.69***	4.68**	2.93**		7.28***	1.23	3.07***
Degrees of Freedom		(1, 90)	(1, 89)	(3, 86)		(1, 90)	(1, 89)	(3, 86)
R²	.16	.23	.27	.34	.19	.25	.26	.34
Adjusted R²	.11	.18	.21	.21	.14	.20	.21	.26

^aStandardized coefficients ^bt-statistics are in boldface; all tests of significance are two-tailed

* $p < .10$; ** $p < .05$; *** $p < .01$

Table 5 Multiple Regression Results: FPC

	Synergistic Gains				Acquirer Wealth			
	Model 1	Model 2	Model 3	Model 4	Model 1	Model 2	Model 3	Model 4
A. Acquirer Brand Resources	.37** 2.07	.37** 2.14	.41** 2.35	.25 1.41	.42** 2.38	.43** 2.51	.45** 2.58	.28 1.61
B. Acquirer R&D Resources	-.23 -1.45	-.29* -1.80	-.29* -1.85	-.28* -1.85	-.29 -1.84	-.37** -2.36	-.37** -2.37	-.36** -2.35
C. Relative Size	.05 .49	.05 .54	.02 .21	.01 .02	.01 .11	.02 .18	.02 .01	.02 -.16
D. Acquirer Strategic Emphasis	.06 .50	.08 .68	.05 .45	.39** 2.28	.01 .08	.04 .33	.02 .21	.38** 2.28
E. Target Strategic Emphasis	-.11 -1.08	-.05 -.51	-.05 -.45	.07 .65	-.09 -.95	-.02 -.20	-.02 -.17	.09 .71
F. Acquirer Strategic Emphasis x Target Strategic Emphasis		.21** 2.07	.20** 1.99	.42*** 2.98		.29*** 2.84	.28*** 2.78	.48*** 3.46
G. Motive			.18* 1.88	.21** 2.15			.09 .90	.11 1.16
H. Acquirer Strategic Emphasis x Motive				-.36** -2.50				-.39*** -2.77
I. Target Strategic Emphasis x Motive				-1.03 -.11				.08 .75
J. Motive x F				-.24** -1.81				-.22** -1.71
F-Value	1.87	2.33**	2.55**	2.85***	1.83	2.98**	2.67**	3.00***
Degrees of Freedom	(5, 96)	(6, 95)	(7, 94)	(10, 91)	(5, 96)	(6, 95)	(7, 95)	(10, 91)
Change in F		4.41**	3.39**	3.68**		6.77***	1.13	5.62***
Degrees of Freedom		(1, 95)	(1, 94)	(3, 91)		(1, 95)	(1, 94)	(3, 91)
R²	.09	.13	.16	.24	.09	.16	.17	.25
Adjusted R²	.04	.07	.09	.16	.04	.10	.10	.16

^aStandardized coefficients ^bt-statistics are in boldface; all tests of significance are two-tailed

* $p < .10$; ** $p < .05$; *** $p < .01$

Table 6 Post-hoc Probes of Three-way Interactions¹⁷

Condition	Focal Parameter	Electronics^a	FPC^a
Step 1: Target Strategic Emphasis High (Marketing-Oriented)	Acquirer Strategic Emphasis * Motive	.85 ^{***}	-.54 ^{**}
Step 2: Target Strategic Emphasis is High (Marketing-Oriented) and Motive is Consolidation	Acquirer Strategic Emphasis	.88 ^{***}	.10
Step 3: Target Strategic Emphasis is High (Marketing-Oriented) and Motive is Diversification	Acquirer Strategic Emphasis	-.41 ^{***}	.59 ^{***}

^aStandard beta

* $p < .10$; ** $p < .05$; *** $p < .01$

Notes: SG = Synergistic Gains, AW= Acquirer Wealth

¹⁷ The Synergistic Gains for Mergers when Target has a Marketing Strategic Emphasis

Table 7 The Impact of Strategic Emphasis Alignment on Accounting Costs (n=75)

	Change in SGA/Sales Ratio
A. Acquirer Brand Resources	0.00 1.23
B. Acquirer R&D Resources	-0.16 -0.70
C. Relative Size	-0.18* -1.86
D. Acquirer Strategic Emphasis	-0.02 .08
E. Target Strategic Emphasis	-0.12 -0.77
F. Acquirer Strategic Emphasis* Target Strategic Emphasis	0.13 .47
G. Motive	0.20* 1.84
H. Acquirer Strategic Emphasis * Motive	0.29* 1.93
I. Target Strategic Emphasis * Motive	0.07 0.63
J. Motive * F	-0.55*** -3.44
F-VALUE	4.50**
DEGREES OF FREEDOM	(10, 62))
R²	.24

^aStandardized coefficients

^bt-statistics are in boldface; all tests of significance are two-tailed

* $p < .10$; ** $p < .05$; *** $p < .01$

Figure 1 The Conceptual Model

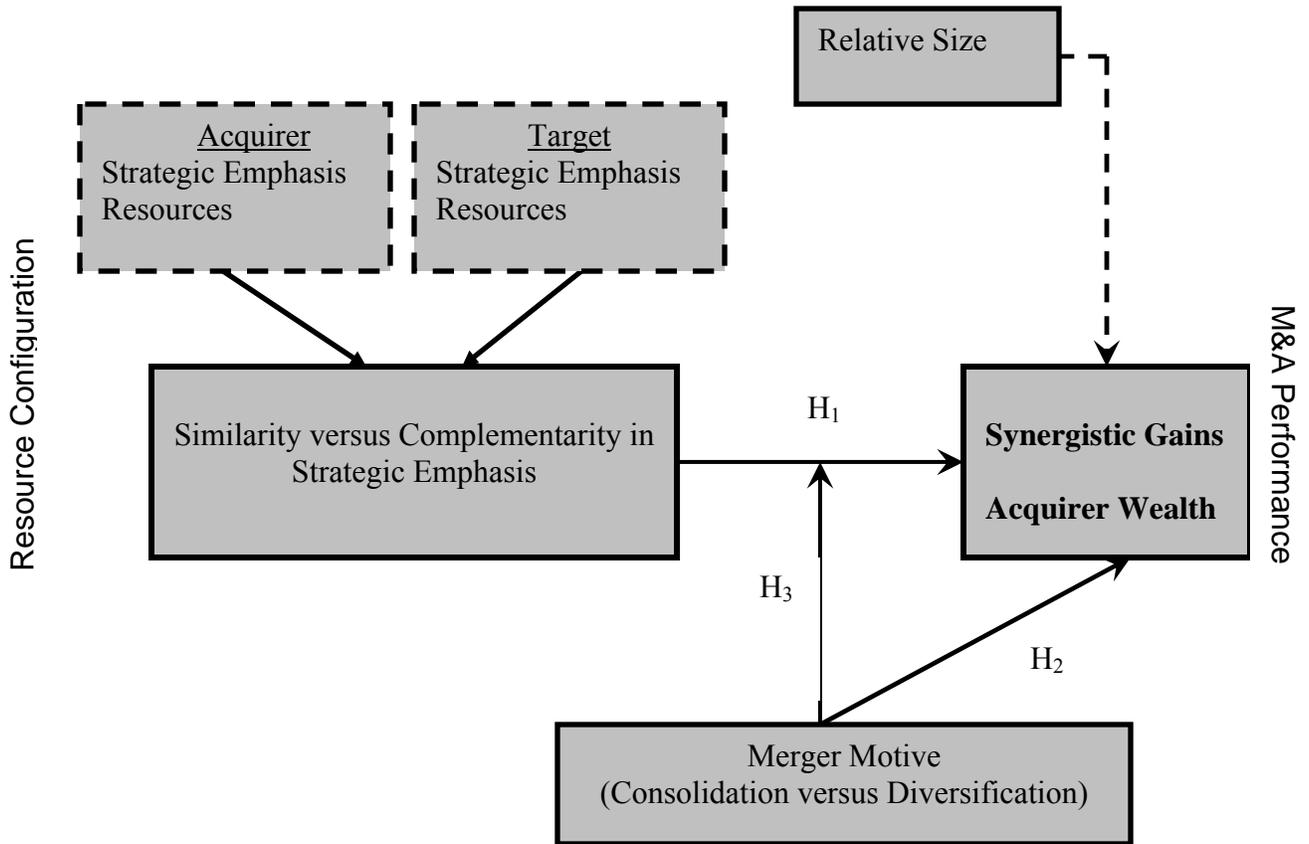


Figure 2 Acquirers' Cumulative Abnormal Returns (CAR): Electronics

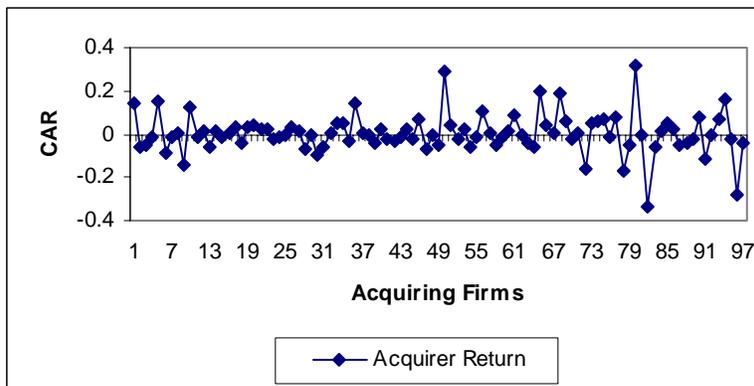


Figure 3 Targets' Cumulative Abnormal Returns (CAR): Electronics

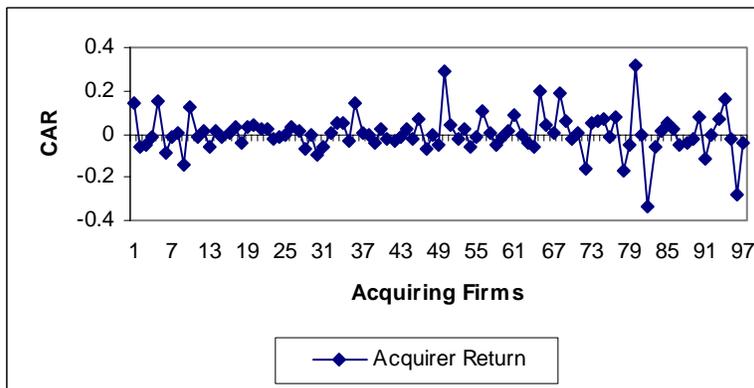


Figure 4 Synergistic Gains from the Merger: Electronics

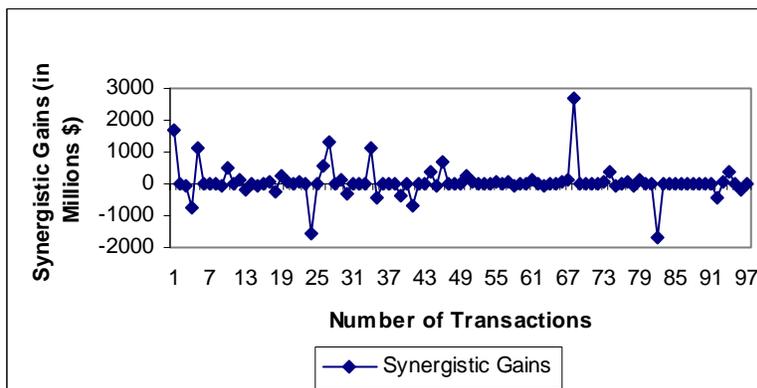


Figure 5 Acquirers' Cumulative Abnormal Returns (CAR): FPC

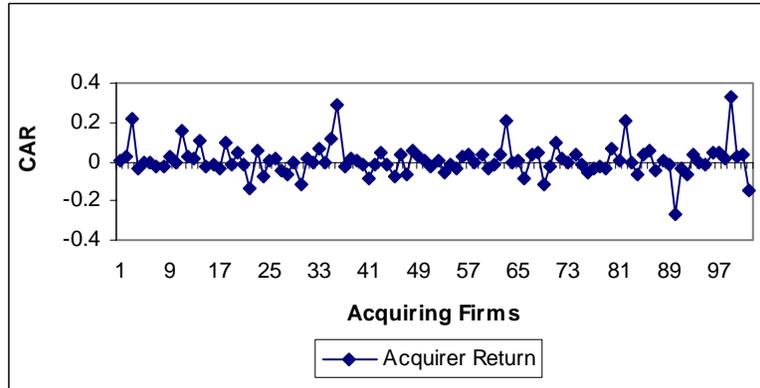


Figure 6 Targets' Cumulative Abnormal Returns (CAR): FPC

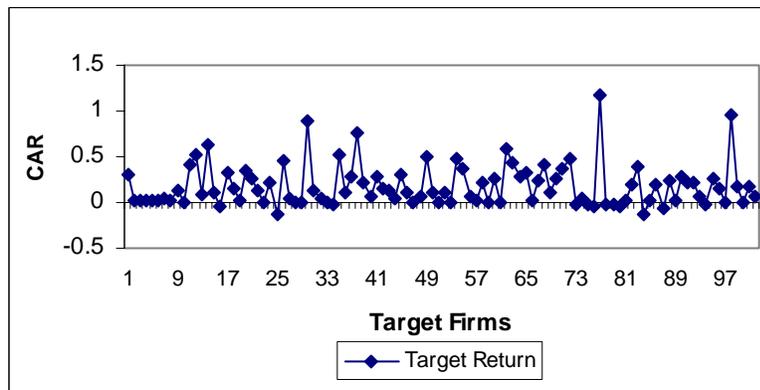


Figure 7 Synergistic Gains from the Merger: FPC

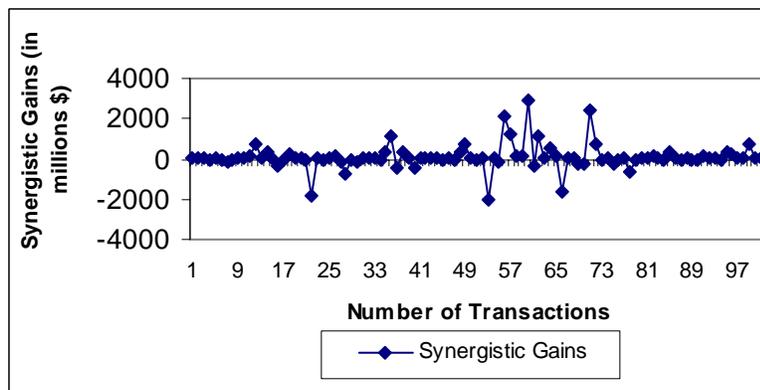


Figure 8 Synergistic Gains under Consolidation Motive: Electronics

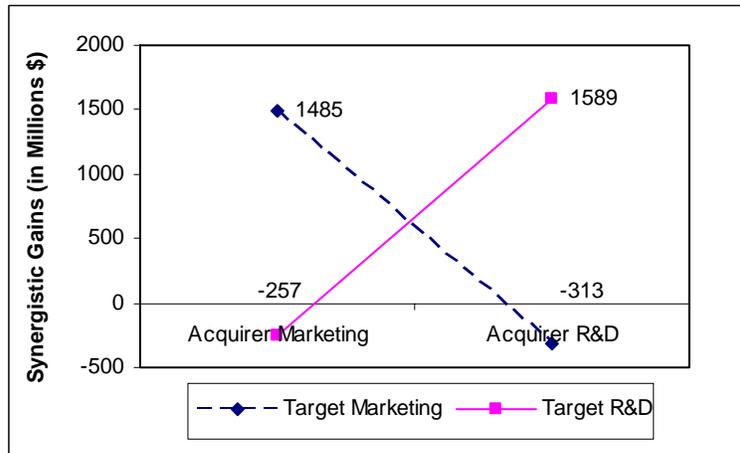


Figure 9 Synergistic Gains under Diversification Motive: Electronics

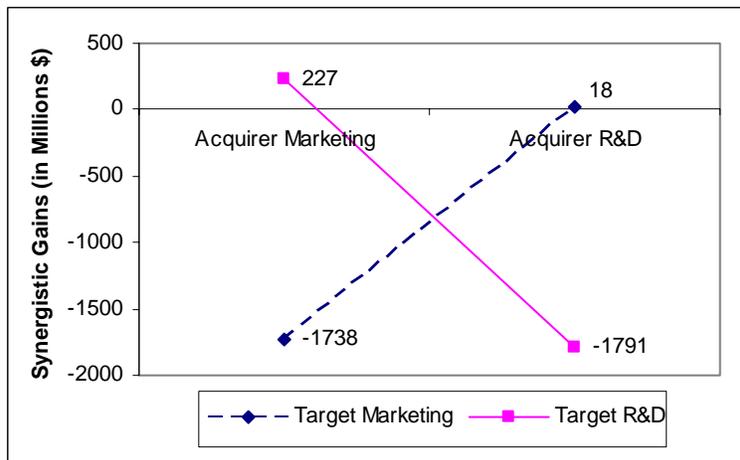


Figure 10 Acquirer Wealth under Consolidation Motive: Electronics

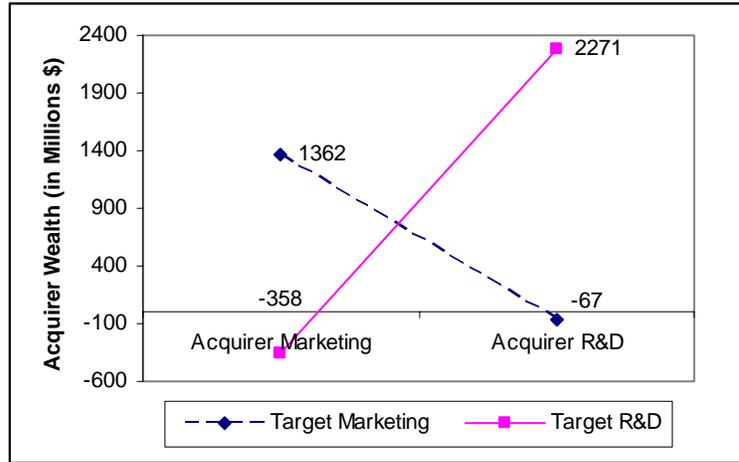


Figure 11 Acquirer Wealth under Diversification Motive: Electronics

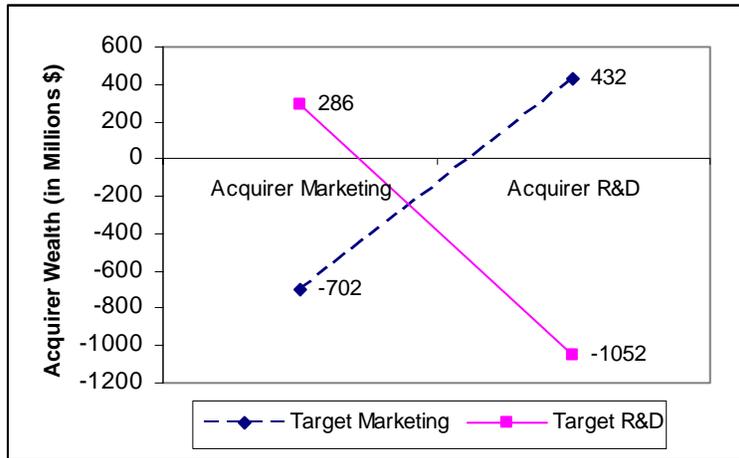


Figure 12 Synergistic Gains under Consolidation Motive: FPC

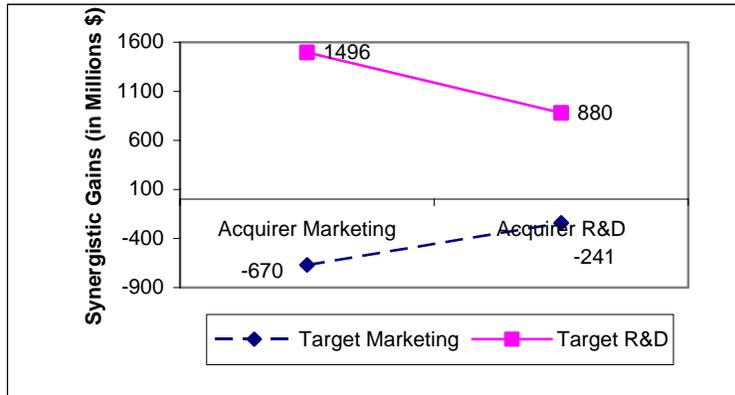


Figure 13 Synergistic Gains under Diversification Motive: FPC

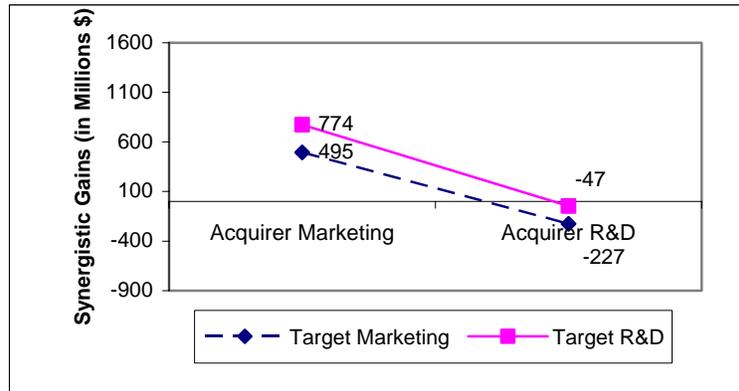


Figure 14 Acquirer Wealth under Consolidation Motive: FPC

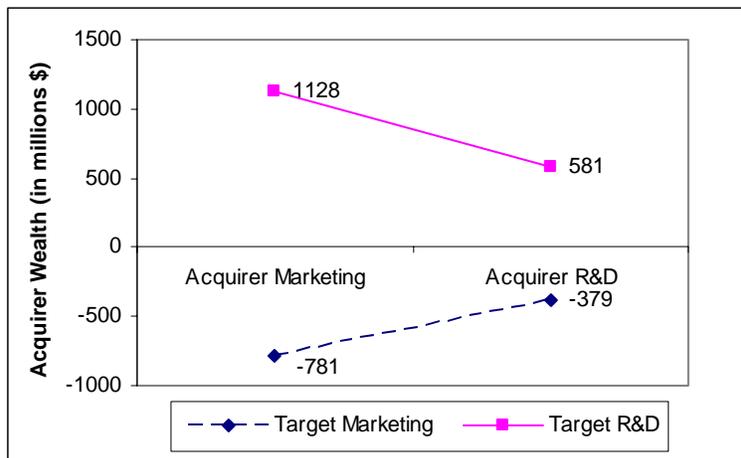


Figure 15 Acquirer Wealth under Diversification Motive: FPC

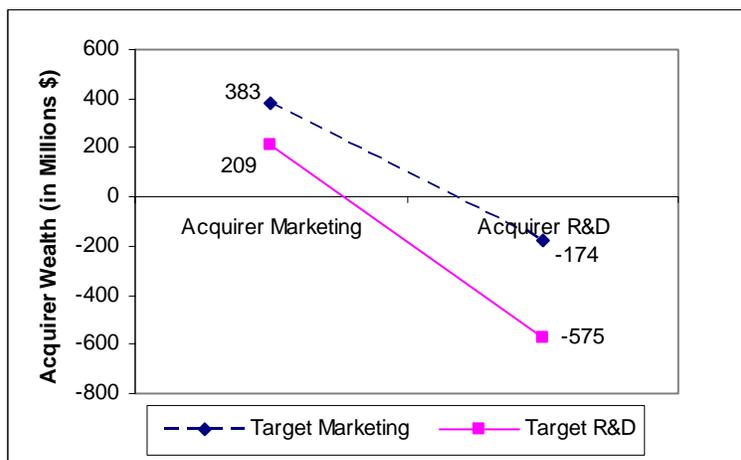


Figure 16 Cost Efficiency under Consolidation: Electronics

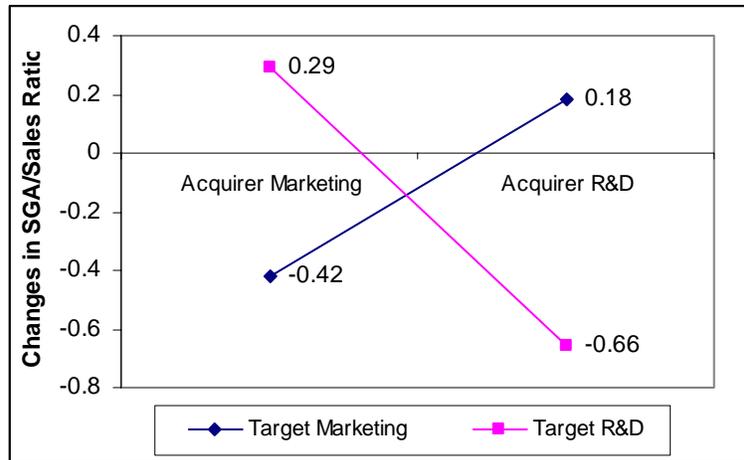
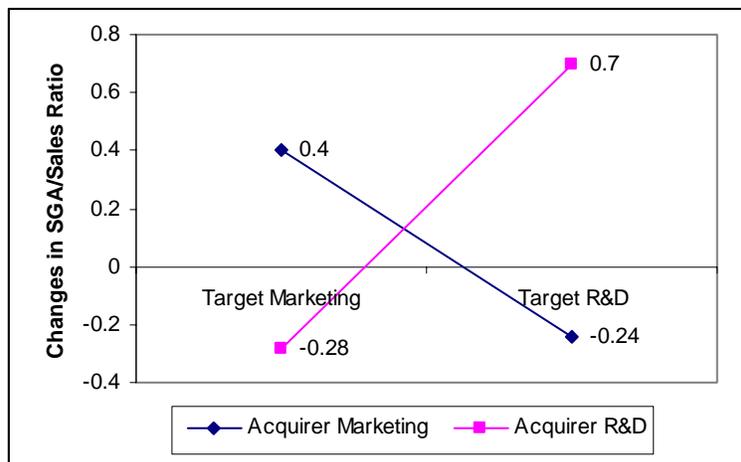


Figure 17 Cost Efficiency under Diversification



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