Understanding success and failure in mergers and acquisitions
McCarthy, Killian

IMPORTANT NOTE: You are advised to consult the publisher's version (publisher's PDF) if you wish to cite from it. Please check the document version below.

Document Version
Publisher's PDF, also known as Version of record

Publication date:
2011

Link to publication in University of Groningen/UMCG research database

Citation for published version (APA):

Copyright
Other than for strictly personal use, it is not permitted to download or to forward/distribute the text or part of it without the consent of the author(s) and/or copyright holder(s), unless the work is under an open content license (like Creative Commons).

Take-down policy
If you believe that this document breaches copyright please contact us providing details, and we will remove access to the work immediately and investigate your claim.

Downloaded from the University of Groningen/UMCG research database (Pure): http://www.rug.nl/research/portal. For technical reasons the number of authors shown on this cover page is limited to 10 maximum.
CHAPTER SIX – MANAGERIAL POWER

“The chance of gain is by every man more or less overvalued, and the chance of loss is by most men undervalued”.

(Smith, 1776)
CHAPTER SIX – MANAGERIAL POWER

‘POWER, AND THE DESTRUCTION OF VALUE IN MERGERS AND ACQUISITIONS *

1. INTRODUCTION

Between 1995 and 1999 nine thousand billion dollars was spent by North American and Western European firms on mergers and acquisitions (M&A); a near incomprehensible figure which, by way of comparison, was about seven times the UK’s GDP, and more then twenty times that of the Netherlands (Schenk, 2003) in the same period. So large was the expenditure that, as a percentage of US GDP, mergers and acquisitions soared from 1.6% in the 1960, to 3.4% in the 1980s, to a staggering 15.4% of at the height of the ‘fifth merger wave’ in 1999 (Mergerstat, 2006). And as the ‘sixth merger wave’ unfolded (2003-2008), records were again broken, when “the value of M&A averaged $10 billion a day” (The Economist, April 8, 2006).

Positive as this may at first appear, the fact that the impact of M&A activity on the performance of the firm is, at best, “inconclusive” (Roll, 1988; Haspeslagh & Jemison, 1991; Sirower, 1997), and at worst “systematic[ally] detrimental” (Dickerson et al., 1997), is nothing short of troubling. Some studies have reported that the combined average returns (CAR) – that is, the average net change in value, accrued to the shareholders of both the acquiring and target company and caused by a merger – are positive but small (Campa & Hernando, 2004). And others still occasionally find no significant effects on performance (Stulz et al., 1990). The “overwhelming majority”, however, find that “M&A activity does not positively contribute to the acquiring firm’s performance” (King et al. 2004), or its profitability, as variously measured (Ravenscraft & Scherer, 1987; Bühner, 1991; Simon et al., 1996; Berger & Humphrey, 1992; Rhoades, 1998). A consensus of estimates places the M&A failure rate somewhere in the range of 65 to 85% (Puranam & Singh, 1999), a figure which Moeller et al (2005) translate into annual losses of $60 billion.

The paradox is that mergers should, however, create value. Because – according to efficiency theory – mergers are an alteration to the boundaries of the firm, which occur either because the manager attempts to cut costs – by internalising those transactions that had previously been negotiated on the market – or to expand revenues – by seeking out scale economies in new products and markets (Besanko et al., 2006). And they will only be concluded when the shareholders of both the target and acquirer possess a symmetric expectation of a realisable gain (Weston et al., 2004). The scale of the destruction thus creates important questions about the effectiveness with which the firm’s boundaries can be altered by the manager.

A number of firm- and deal-specific explanations have been put forward to explain why mergers fail. Chatterjee (1986) and Gugler et al. (2003), for example, show that the ‘degree of relatedness’ between the target and the acquirer is a

significant explanatory variable in predicting post-merger performance. Moeller et al. (2004) and, more recently, Weitzel and McCarthy (2010), show that size matters, and find that larger acquirers underperform their smaller rivals, while Officer (2007) and Chang (1998) provide evidence that acquirer returns in publicly listed targets differ significantly from private targets. Jensen (1986; 2003) shows that the presence of ‘free cash’ (or excess liquidity) affects performance, because it liberates the firm from the so-called ‘discipline of debt’; a conclusion confirmed by Hitt et al. (1998) from the perspective of leverage. Carlino et al. (2002) finds significance in deal values, suggesting that the bigger the deal the poorer the performance, and Moeller et al (2005) finds that merger waves significantly impact average deal value. Haunschild (1994), Hayward & Hambrick (1997), and Hitt & Pisano (2003) all find evidence that the payment of ‘premiums’ – that is, the payment of a sum on top of the firms market value – predicts poor performance, while Betton & Eckbo (2000) and Jensen & Ruback (1983) find that hostility also plays an important role in merger success.

In this paper we introduce the managers’ ‘experience of power’ as an explanation for the observed destruction of merger value. We argue that the extant literature adopts a predominately finance-orientated perspective in attempting to understand success and failure – within which it is assumed that mergers and acquisitions are a ‘closed system’ – with little room for human influence or interference. We suggest, however, that managers have unique opportunities to create or destroy value in the conclusion of a merger, owing to their position of power. And adopt a multidisciplinary approach to understanding and predicting success and failure, by synthesizing new research on the impact of power on judgment and decision making with existing research on mergers and the merger process.

We begin, in Section Two, with a review of the merger process, within which we consider the explanations – both financial and psychological – for why mergers destroy value. In Section Three, we examine ‘managerial power’ – a psychological factor known to affect key aspects of judgment and decision-making – as an important and yet unexplored element of value creation (and destruction) and, in Section Four, we then build a conceptual model, which systematically describes how power affects value. In Section Four we identify the limitations of our analysis, and suggest some practical implications of our theoretical model in light of these limitations, and in Section Five, we conclude with a discussion of our future research directions.

2. UNDERSTANDING MERGERS AND ACQUISITIONS

2.1 The Merger Process

The various stages of the merger process can be described as the: “pre-merger” (planning), “during-the-merger” (realization), or “post-merger” (integration) stages (Appelbaum et al., 2000; Cartwright & Cooper, 2000; Jansen & Pohlmann, 2000). To understand the scope of managerial power, it is necessary to understand each stage.

The ‘pre-merger’ stage consists of a number of ‘planning’ and ‘positioning’ decisions (see Figure 1). The decision to merge is made by a few top executives – if not a single CEO or Chairman – who makes a decision either to cut costs, by internalising operations that had previously been negotiated on the market, or to expand revenues, through the attainment of scale economies. ‘Searching’ and ‘screening’ (that is, the ‘due-diligence process’) come next, as target companies are considered on the basis of their projected earning potential and strategic fit (be it in products, markets, location, and resources). And based on the (legal and financial) health of these companies, negotiations top level negotiations then begin.
The contract is signed in the “during-the-merger” phase. During this phase ‘integration planning’ also occurs (Burgelman and Grove, 2007), redundancies are defined, and the merger announcement is planned and then executed.

In the ‘post-merger’ phase strategic capabilities are integrated, in an effort to realize synergies, and thereby create value. This stage involves strategic interactions between the managers of different hierarchical levels, and between colleagues of partner organizations. Effective communication, an understanding of and respect for each other’s organizational structure and culture are essential for the transfer and integration of capabilities, and the creation of value (Haspeslagh & Jemison, 1991).

Figure 1: The M&A Process

2.2 Merger Motives & the Destruction of Value

Synergistic savings and economies in scale and scope – and thus the creation of value – are amongst the most commonly cited merger motives (Gaughan, 2007).

A merger of two firms is thought to result in: (a) cost synergies, as labour forces are reduced, and administration and production costs are streamlined (Carey, 2000); (b) market power gains, as a reduction in the level of competition allows for wealth to be transferred from the firms customers and suppliers to its shareholders (Chatterjee, 1986); (c) financial gains, as a merger produces a company with a reduced tax profile (Devos et al., 2008); (d) scale and scope economies, as firm exploits the opportunity to expand and diversify into new products and regions (Besanko et al., 2006).

There are, however, also subtle psychological reasons for mergers, that are widely unacknowledged but implicitly understood (Cartwright & Cooper, 1990).

Fear of obsolescence, personal interest, and the desire for power, prestige and empire are examples of such psychological motives (Schleifer and Vishny, 1989). Each is connected to the managers’ egocentric needs to increase or maintain personal power; indeed several scholars and independent consulting firms have recognized that
M&As are often born out of the ‘personal whims’ of egotistical CEOs, looking for excitement, a feeling of control or influence over the direction of the company, the need to gain collective influence, to entrench themselves in an irreplaceable position within the firm, or simply following an urge for empire-building (Cartwright & Cooper, 1990; Haloern & Western, 1983; McKinsey & Associates, 1988).

It is perhaps not surprising that mergers motivated by economic considerations – that is, by the attainment of ‘synergies’ – are generally more successful than those motivated by ego-protection or agency (Weitzel & McCarthy, 2010). But studies suggest that even these often fail to produce non-negative returns (Martynova & Renneboog, 2008; Appelbaum et al., 2000; Cartwright & Cooper, 1993).

There are several reasons for why mergers might fail (Trautwein, 1990). Understandably, many of these have to do with failures in the strategic, financial and economic decision-making processes. For example, an under-privileged due-diligence analyses, poor selection decisions, a lack of pre-planning, a strategic and financial mismatch, a failure to correctly estimate the value of the target, and unpredicted changes in market conditions can all contribute to poor performance (Cartwright & Cooper, 1990; Fairburn & Geroski, 1989; Rockness et al., 2001). And a number of firm- and deal-specific characteristics – such as size, relatedness, and ownership structure, the levels of hostility, liquidity and methods of payment – have been found to play an important role in moderating the probability of success and failure.

Human factors, however, and the psychology of the manager, are a much-neglected explanation for the destruction of value, because it is assumed that mergers are a ‘closed system’, with little room for human influence or interference. Estimates suggest, however, that the manager may be responsible for between one third to one half of all merger failures (Cartwright & Cooper, 1990; Dannemiller Tyson, 2000).

2.3 The Psychology of the Manager

The manager can influence and undermine the M&A process at both the pre- and post-merger stages (see Weitzel and McCarthy, 2010 for an overview).

Managerial influence on pre-merger processes. A number of theories explain value-destruction at the pre-merger stage. The theory of managerial hubris (Roll, 1986) for example, suggests that managers may have good intentions in initiating mergers, and that they may aim to increase the value of the firm. The theory suggests, however, that being over-confident, managers typically over-estimate their abilities to create synergies. Over-confidence leads to overpaying (Hayward and Hambrick, 1997; Malmendier and Tate, 2008), which in turn dramatically increases the probability of failure (Dong et al., 2006). By contrast, Jensen’s (1986) theory of managerial discretion claims that it is not managerial over-confidence that drives unproductive acquisitions, but rather the over-confidence of shareholders in managers. Jensen suggests that this allows them to make quick strategic decisions, and to engage in large-scale strategic actions with little analysis or accountability (Martynova and Renneboog, 2008). The managerial theories of the firm (Marris, 1964) are, however, less kind. They suggest that managers may intentionally act as value-destroyers, because they pursue self-serving acquisitions. The theory of managerial entrenchment (Shleifer and Vishny, 1989), for example, claims that unsuccessful mergers occur because managers make investments that minimize the risk of replacement, or allow for increases in wealth, power, reputation and fame.

Managerial influence on post-merger processes. Irrespectively of their initial motivation, the goal of the post-merger processes is to integrate the two organizational structures and cultures. And here the potential for value-destruction is
immense (Burgelman and Grove, 2007). Critical to the success of this stage is the managers’ capacity to effectively communicate organizational goals across hierarchical levels, and between organizations. And an understanding and respect for the organizational structure and culture of both the target and acquirer are essential for an effective transfer and integration of capabilities (Hanspach & Jemison, 1991). It is perhaps no surprise, therefore, that failures at this stage have been attributed to the absence of emotionally intelligent leadership (Cartwright & Cooper, 2000).

2.4 A Gap in the Literature

Clearly, the manager occupies a position of power, and can influence both the organisational strategy of the firm, and group decision processes, to destroy value. And yet little is known about the manner in which the manager affects value in mergers and acquisitions, beyond the fact that hubris, or motives for self-protection (entrenchment) or self-enhancement (empire-building) destroy value. There is therefore an important gap in our understanding of the psychology of the manager. The goal of the present research is to correct this, and to investigate ‘power’ – a psychological factor known to affect key aspects of judgment and decision-making – as an important and yet unexplored element in the creation and destruction of value.

3. The Impact of Managerial Power on the M&A Process

It has been empirically demonstrated that individuals in a position of power have a unique capacity to affect the thoughts, feelings, and even behaviours of others. More recent research reveals that the ‘experience of power’ itself has the capacity to influence the thoughts, feelings, and behaviours of powerful individuals themselves, often to destructive ends. Put another way, individuals in a position of power are influenced by it to think and act in ways that they would not otherwise. In this section, we consider the nature of managerial power, and explore how this can affect judgment and decision making processes, that are critical to M&A processes.

3.1 Power Affects Thought and Behavior

Power is ‘experienced’ when individuals have asymmetric responsibility for and control over valued resources in social relations (Fiske, 1993). Managers, responsible for the division of a firm’s resources to a greater extent than other organizational members, are thus in a position associated with the experience of power.

The potential for power to influence managerial judgment and decision making processes stems from the fact that power fundamentally alters individuals’ psychological states. The most influential and empirically-supported theoretical framework for understanding the psychological effects of power is known as the ‘power approach theory’ (Keltner, Gruenfeld & Anderson, 2003). This theory posits that elevated power activates what social psychologists refer to as the ‘behavioral approach system’ – which increases ones sensitivity to rewards – while powerlessness activates the so-called ‘behavioral inhibition system’ – which triggers a sensitivity to threats. Although at first both are probably unfamiliar, we suggest that both will have been experienced by the reader: in response to positive environmental feedback.

---

2 Take for instance, Milgram’s classic study (1963) in which participants obediently delivered what they thought were 440-volt shocks to anonymous strangers at the insistence of an experimenter – a person in a position of relative power. People in a position of power, it was shown, are capable of influencing the decisions and behaviors of others, to destructive ends.
(receiving praise, for example), one feels motivated to approach, or to take action towards the achievement of our goals; in response to negative environmental feedback (receiving criticism, for example), one becomes more inhibited, and proceeds with caution and consideration. Thus the activation of behavioral systems will vary from situation to situation. However, people in a position of power, it is suggested, will more often than not find themselves in an approach-state rather than inhibition-state.

The power-induced activation of the behavioral approach system has important cognitive and behavioral consequences. In the following, we will discuss how the experience of power: (1) increases the individual’s attention to rewards and opportunities, and decreases his attention to threats; and (2) reduces social attentiveness. These effects are particularly important in the context of mergers and acquisitions, where vigilant decision-making, and behavioral caution, reduces the potential for errors in the pre-merger planning and post-merger integration stages.

3.1.1 Attention to opportunities and rewards

A host of research – directly flowing from this power-approach theory (Keltner et al., 2003) – has shown that the powerful appear to be optimistic, action-oriented individuals, prone to overconfidence, risk-taking, and illusions of control.

**Power Increases Optimism and Risk-Taking.** Research has shown that power induces a general sense of optimism. Powerful individuals, it has been shown, tend to believe that their future holds both more positive and less negative events in store for them (Anderson & Galinsky, 2006). These optimistic views of the world increases the attraction of the powerful to risk, both in terms of exhibiting greater risk preferences as well as in making riskier choices (Anderson & Galinsky, 2006; Maner, Gailliot, Butz, & Peruche, 2007). The risky decision-making and behavior of the powerful is also facilitated by their tendency to focus their attention on the potential rewards, rather than the potential threats in their environment. When presented with a selection of alternatives, therefore, they are more likely to see the potential gains associated with each option, and to become blind to the potential losses.

**Power Increases Illusions of Control.** Power not only transforms individuals into optimists and risk-takers, it also increases their general sense of control. Even in situations where this control is illusory. In other words, powerful people are more optimistic, and take more assertive action, because they experience a heightened sense of control. This sense of control can, however, result in both positive and negative downstream consequences. For instance, illusion of control allows the powerful to achieve seemingly unreachable goals, by pursuing low probability alternatives and (Taylor & Brown, 1988). But as pointed out by Galinsky et al. (2010), the relationship between power and illusory control might also contribute to an escalation of commitment, leading themselves and others down disastrous paths of entrapment.

3.1.2 Social attentiveness

Perhaps because they are less reliant on others for access to valued resources, people in a position of power are less attentive to the thoughts and feelings of others (e.g. Galinsky, McGee, Inesi, & Gruenfeld, 2006), and are less concerned with social norms. Unless, of course, these others are seen by the powerful to be instrumental to the achievement of self-interested goals, in which case they show increased attentiveness to the thoughts and feelings of others (Overbeck & Park, 2006).

**Power reduces perspective-taking and compassion.** The powerful are notoriously poor perspective-takers. Galinsky et al (2006), for example, found that the
powerful are less able to take the visual perspective of others, to take others’ background knowledge into account, and to correctly identify others’ emotional expressions. This lack of understanding of others’ point of view and feelings impairs communication. Research has shown that power also impairs compassion, however, and blinds people to the feelings of others. The powerful are less accurate, it has been shown, in comprehending others’ emotional states (Galinsky et al, 2006), and show diminished reciprocal emotional responses to another person’s suffering (feeling distress, for example, at another person’s distress). Van Kleef et al (2008) found that the powerful’s emotional disengagement from others was driven by power-related differences in the motivation to affiliate with and connect with others.

There is, however, one caveat to this: power makes people more inclined to view others in an instrumental manner, as a tool toward the achievement of their own goals. For example, a series of studies by Overbeck and Park (2006) showed that when the powerful are pursuing “people-centered” goals they individuate their targets by paying increased attention to and remembering more unique information about them. Similarly, Gruenfeld and colleagues (2008) found that power increases objectification, which they define as relating to social targets, based on their utility for achieving self-relevant goals. As we discuss below, this tendency for powerful individuals to view others in an instrumental manner can have both positive and negative consequences for the realization of value in the M&A process.

The powerful think abstractly. Finally, Smith and Trope (2006) found that the powerful engaged in more abstract thinking than the powerless, who demonstrate more concrete thinking. Abstract thinking is used to identify the relationship between the individual parts and the whole – it is the ability to see the big picture, or the forest for the trees. Concrete thinking, on the other hand, is detail-oriented. Thus, Smith and Trope (2006) found that the powerful are better able to recognize patterns in the environment and capture the gist of large amounts of information efficiently and effectively. But are often less capable of effectively operationalizing their plans.

3.1.3 On the effects of Power on Thought and Behaviour

In sum, we suggest that the manager’s ‘experience of power’ activates the behavioral approach system, which: (1) increases his attention to rewards and opportunities, promoting overconfidence, risk-taking, and an illusion of control; and (2) reduces his social attentiveness, which impairs perspective-taking, compassion, but increases divergent and abstract thinking. We now turn to the implications of these cognitive and behavioral consequences of power for the management of the M&A process, in an effort to better understand the creation and destruction of value.

3.2 Managerial Power in the Merger Process

3.2.1 Power in the Pre-Merger Stage

As outlined in Figure 1, the pre-merger stage involves planning an acquisition, searching, and screening, and results in the selection of a firm with which to merge. Contact is then made, and negotiation are held between top managers on the terms of

---

3 Galinsky et al (2006) presented participants with a scenario in which a individual responded to a very bad restaurant experience by remarking that it was a “marvellous experience. Just marvellous”. The powerful inaccurately predicted that others would see the world as they saw it (i.e., that the message was sarcastic) even though these others lacked access to the private knowledge of the experience.
the merger or acquisition, followed by integration planning, and closing.

Several of these steps may be critically affected by the psychology of the manager, who is in a position of power and therefore may be prone to power-related biases (opportunity-seeking and social inattentiveness). We have also established that the manager’s psychological state is largely affected by his or her experience of power, which increases attention to opportunities and rewards. This attentional bias towards rewards rather than threats may lead to overconfidence (hubris), which motivates managers to enter into mergers and make acquisitions that are high-risk. Indeed, power is also associated with optimism and high-risk decision-making, as managers in a position of power experience an illusion of control over the outcomes of their decisions. Berkovitch and Narayanan (1993) find strong evidence of hubris in US takeovers, and Goergen and Renneboog (2004) find the same in a European context. The latter estimate that about one third of the large takeovers in the 1990s suffered from some form of hubris. Malmendier and Tate (2005) show that overly optimistic managers, who voluntarily retain in-the-money stock options in their own firms, more frequently engage in less profitable diversifying mergers. And Rau and Vermaelen (1998) find that hubris is more likely to be seen amongst low book-to-market ratio firms – that is, amongst the so-called ‘glamour firms’ where managerial discretion is greater – than amongst high book-to-market ratio ‘value firms’. Thus, we suggest that power may motivate managers to enter into mergers that have a high risk of failure, thereby increasing the potential for value-destruction from the outset.

Whatever the motive, once a merger or acquisition has been planned, managers search and screen potential candidates for the merger. Optimally, this process is systematic and detail-oriented. Power interferes with concrete thinking, however, and detail-oriented processing, and hence may impair the managers’ attention to detail in the search and screening process. The rise of management theory, and the idea that ‘good managers can manage anything’ (Weston and Mansinghka, 1971; Gaughan, 2007), it is generally agreed, further diminished the managers attention to detail in the 1960s, and inspired the third merger way (ca. 1960 to 1969) to diversify. In this case, and in any subsequent case where the manager does not pay adequate attention, the suggestion is that power increases the potential for value-destruction, by undermining the process by which the manager chooses a firm with whom to merge or acquire.

After the target has been selected, and – typically informal – first contact with the chosen firm has been made, the negotiation process begins – in which a buying price is settled – begins. Research by van Kleef et al (2006) demonstrates that in the realm of negotiation, power has the potential to facilitate the creation of value. As mentioned above, power reduces social attentiveness; the powerful are better able to turn a blind eye to the suffering of others. Consequently, power protects negotiators from being swayed by the strategic displays of emotions that are designed to induce concessions. Thus, high-power negotiators are less likely to concede to an angry opponent compared to low-power negotiators (Van Kleef et al., 2006). Similarly, in a bargaining context, high-power negotiators are more likely to make a first offer compared to their less powerful partners (Magee et al., 2007). These studies showed that by making the first offer, the powerful garnered a distinct financial advantage. Thus, in the negotiation phase of the M&A process, the power bestowed upon the manager may, we suggest, impart a distinct organizational advantage.

Finally, and as argued by Cartwright & Cooper (2000), many mergers and

---

4 Burgelman and Meza (2004), in describing the merger between Compaq and HP, report (p.5) that:
“...Compaq’s CEO, Michael Capellas, called HP’s CEO, Carly Fiorina, to discuss a joint research and development (R&D) deal, but the conversation turned to acquisition”.

146
acquisitions fail due to poor integration planning. Organizational and cultural clashes, duplication, and a failure to streamline the operation of the firm can all result in the destruction of significant value (Weston et al., 2004). Given that power reduces social attentiveness, and in particular leads to poor perspective-taking and a tendency to view others in an instrumental manner, it is likely that managers experiencing power may be pay less attention to this aspect of the M&A process than necessary for a smooth post-merger integration. Thus, value can again be destroyed in this stage too.

3.2.2 Power in the Post-Merger Stage

In the post-merger stage, the manager oversees the integration of skills and resources necessary for the achievement of synergies, and the creation of value.

The integration stage involves retrenchment and re-allocation of employees, as well as hiring of new middle managers. As discussed earlier, the success of this stage depends on the effective communication of organizational goals within and across organizations. Managerial communication is potentially impaired, however, by the experience of power, which leads individuals to focus on ‘the gist’, and to address problems at a higher level of abstraction, which can lead to communication distortions between high and low power individuals, who tend to think more concretely.

We have seen, however, that managers with enhanced abstract thinking capacity have the ability to see the big picture. Coupled with optimism, this can be used to generate and successfully communicate ‘grand visions for the future’, and thereby motivate subordinates to pursue a common goal. Hence, while power is, in general, an obstacle to communication, it may also facilitate motivational leadership.

As demonstrated by Galinsky et al (2008), however, we have suggested that the powerful have a reduced capacity for perspective-taking which results in a tendency to assume that others have access to private knowledge. In a merger process, this would inevitably impair the communication of details that are essential to employees’ understanding of the situations and problems that arise amidst organizational change.

Destructive as it may be in terms of communication, it is possible that the experience of power can have positive consequences for the merger, in terms of hiring decisions. Gruenfeld et al. (2008) create a hiring situation, in which some job candidates were better fits for specific positions (e.g., a salesperson needed to be extroverted). In this situation high-power individuals were better able to select the candidate whose attributes best matched the hiring criterion. In addition, managers may be better able to make difficult restructuring decisions (i.e. laying off employees), because of their instrumental view of organizational members. In support of this, Lammers and Stapel (2009) found that in a medical simulation, high power senior surgeons’ more object-like view on patients helped them to administer a painful but effective medical treatment. Low power nurses and junior surgeons were hindered from doing so, because they focused too much on the pain and suffering caused by it. Thus, while the relationship between power and objectification might be dysfunctional for social relationships and communication with lower-level managers and employees, it may be functional for the attainment of organizational goals.

Finally, we suggest that managerial power is most likely to affect the evaluation of merger success, and re-evaluation of integration plans, by biasing managers towards the perception of opportunities and rewards and hindering attention to threats and obstacles. Paired with an illusion of control, the powerful may see real threats as mere ‘setbacks’, influencing their willingness to re-evaluate pre-merger integration plans. This promotion- rather than prevention-focused interpretational bias maximizes, rather than minimizes, we suggest, the potential for value-destruction.
3.2.3 On the Effect of Power on the Merger Process

In summary, we suggest that managerial power may influence the M&A process by: introducing overconfidence to the merger motives (value-destruction); reducing the rigor of the search and screening process (value-destruction); facilitating negotiations and bargaining (value-creation); reducing motivation to invest in integration planning (value-destruction); impairing the communication of organizational strategies (value-destruction); enhancing the communication of organizational goals (value-creation); aiding the objectivity with which restructuring (hiring and firing) decisions are made (value-creation); and placing a positive-bias on the evaluation of post-merger processes (value-destruction). These, and the potential, practical, consequences of them on the merger, are documented in Table 1.

Table 1: The Effects of Power on the Merger Process

<table>
<thead>
<tr>
<th>Psychological Construct</th>
<th>Effect on the Merger Process</th>
<th>Effect on Shareholder Value</th>
<th>Merger Stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Over confidence in the initiation of an (ill-advised/unnecessary) merger</td>
<td>-</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Reduced search and screen</td>
<td>-</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Facilitated Negotiation and Bargaining</td>
<td>+</td>
<td>5 &amp; 6</td>
<td></td>
</tr>
<tr>
<td>Failure to Plan for Integration</td>
<td>-</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Impaired Ability to Communicate Strategic Strategies</td>
<td>-</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Enhanced Ability to Communicate Organisational Goals</td>
<td>+</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Increased Objectivity in Restructuring (hiring and firing decisions)</td>
<td>+</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>Positive Bias in the Evaluation of the Merger</td>
<td>-</td>
<td>10</td>
<td></td>
</tr>
</tbody>
</table>

Thus, while power clearly provides managers with key competencies in the negotiation of the merger, the communication of organizational goals, and strategic restructuring, there are several phases of the M&A process that may be undermined by managerial power, if that power is allowed to lead organizational policy unchecked. In the next section, we discuss strategies for utilizing managerial power in mergers, and strategies for managing the influence of the powerful in the M&A process. Firstly, however, it is important to address the limitations of our analysis for understanding the impact of managerial power on mergers and acquisitions.

4. Discussion

4.1 Theoretical Limitations

Our preceding discussion of the effects of manager power on M&A success suggests that it can increase the probability of value-destruction in many ways due to
the fact that power increases attention to rewards or opportunities and decreases social attentiveness. An important caveat to this perspective, however, is that while power has these effects, in general, there are certain individuals that will be immune to these effects of power. Indeed, there are certain groups of individuals for whom power only serves to increase attention to threats and attention to social relationships.

4.2 Individual differences in manager psychology

Recent research lends credence to Lincoln’s intuition that “nearly all men can stand adversity, but if you want to test a man’s character, give him power”.

Research indicates that power increases the correspondence between individual traits and behavior (Galinsky et al., 2008), with their personalities being better predictors of their thoughts and behaviors than are the personalities of the powerless. The implication of this is two-fold: (a) the effects of power should be attenuated by the possession of personality traits that are inconsistent with the general effects of power on people; and (b) the effects of power should differ across cultures that vary in their conceptualizations of the self in relation to others (Zhong et al., 2009).

A number of recent studies have provided support for the idea that power reveals the person’s true personality. Chen et al. (2001) found that so called ‘communally-oriented people’ act more selflessly, and ‘exchange-oriented people’ act more selfishly, when allowed to experience power. The authors argued that power activated social responsibility goals in ‘communals’, and self-interest goals in ‘exchangers’, thus leading to different behavioral outcomes. Similarly, Galinsky et al. (2008) found that in a negotiation task, high power participants’ social value orientations were better predictors of their interest in trusting and building a relationship with their negotiation partner than their partners’ reputations. In contrast, baseline participants’ interest in relationship building was more a function of their partner’s reputation than of their social value orientations. In sum, the behaviors of the powerful will be in line with their personality when these personality traits conflict with the expressions of power exhibited by the general population.

Individual differences that are rooted in culture have also been shown to moderate the effects of power on cognition and behavior. Zhong et al (2009) shows that the effects of power on attention to rewards are culturally bound: whereas Western cultures automatically associate power with freedom and reward, Eastern cultures automatically associate power with restraint and responsibility. The implications of this is that Western managers in a position of power show an attentional bias towards rewards, while Eastern managers may show attention to responsibilities and potential threats to organizational performance. Furthermore, members of Western and Eastern cultures differ in their construal of the “self”; Western cultures stress the autonomy and separateness of the self, whereas East Asian cultures tend to have interdependent self-construals, that emphasize the importance of social connectedness and of being embedded in larger groups. Thus, Galinsky et al. (2003) finds that among Westerners power increases self-interested claiming in a commons dilemma. In contrast, Zhong et al. (2009) showed that among East Asians, power led to reduced claiming from a commonly shared resource pool.

In sum, while there are consistent and predictable effects of power on cognition and behavior observable amongst the general population, there are certain individuals, and groups, that will tend to reveal power differently. As discussed below, the moderating role of personality and culture on the effects of power are important to keep in mind when considering the management of power in the M&A process.
4.2 Practical Implications

With a new-found understanding of the potential for power to influence managers’ thoughts and behaviors in destructive ways at specific stages of the M&A process, it is clear that management need to be managed during the M&A process. In particular, based on our forgoing review and synthesis of research on power and merger processes, we can identify four key phases of the M&A process in which the negative effects of power on managerial decision making can be curbed.

1. *The acquisition plan should be checked for signs of overconfidence or hubris.* Our results show that powerful managers are likely to be overly optimistic in their decision to merge, taking on ‘hopeless cases’, or paying ‘premiums’, even when ‘premiums’ drastically increases the pressure on the acquiring firm to create returns (Haunschild, 1994; Hayward & Hambrick, 1997), and are thought to be *per se* excessive (Hitt & Pisano, 2003; Kirshnan et al., 2007).

2. *The search and screening process should be carried out by less-powerful organizational members.* Our results show that powerful individuals rely more on abstract thinking, and are less detail orientated, both of which undermines the process by which a manager chooses a firm with whom to merge or acquire. Coupled with the out-dated idea that a ‘good manager can manage anything’ (Weston and Mansinghka, 1971), this can lead to a merger of poor strategic fit, and may be used as an explanation for why mergers by ‘glamour acquirers’—planned by liberated, independent and empowered managers—typically perform less well than ‘value firms’—concluded by managers clearly supervised by the firms other stakeholders (Rau & Vermaelen, 1998).

3. *Integration planning and post-merger integration management should be drafted by a HR manager or external organizational consultant, who understands the importance of cultural integration and communication of organizational goals, and is at the same time sufficiently independent from the employees to guard against sympathetic rather than efficient restructuring.* Our results show that powerful managers are good at communicating the ‘bigger picture’, but not the methods by which this might be attained. Powerful managers are good at cutting costs—possibly explaining why workforces are often so ruthlessly cut in mergers (e.g., Krishnan et al., 2007)—but poor at perspective taking, paying little attention to the ‘human side’ of integration planning. A HR manager, we suggest, would bridge the gap between the “big picture” of the manager and the concrete perspective of the employees, taking into account both the culture of the acquirer and the acquire. As the failure to do so is a chief reason for merger to go sour.

4. *Post-merger evaluation process should be undertaken by the manager, in cooperation with lower-level managers, and a third-party consultant, in order to objectively check the reliability of the evaluations.* Our results show that egotism and optimism are likely to lead the manager to judge his failures with bias, and to consider real threats to the long-run sustainability of the firm as

---

5 A ‘premium’ is a proportion of the expected synergy gain from the combined firm, which is paid to the target and offered in excess of the firm’s stand-alone valuation (DePamphilis, 2005).
little more than short-term setbacks. This is an obvious threat to the firm, as ‘those who do not learn from their mistakes are destined to repeat them’.

The ideal approach to the management of power in the M&A process would be to recruit a manager with a personality profile that would capture the value of power at the negotiation and integration (restructuring) phases, without compromising value at the planning, searching and screening, integrating (communication), and evaluation stages. Identifying the selfish, the harassing, and the volatile is critical for creating value efficiently and effectively in mergers and acquisitions. Managers of the M&A process cannot, we suggest, simply be technical experts or analytically skilled, but must also be individuals who take their group members’ perspectives, who value their relationship with their peers and subordinates, and who derive self-esteem by enhancing the well-being of others, rather than relying on self-enhancing strategies such as empire building for self-esteem and a sense of personal security.

Another possibility, however, would be to heighten the risk-perception and social attentiveness of the powerful. One possible way to increase perspective-taking would be to hold the powerful accountable (Tetlock, Skitka, & Boettger, 1989). Powerful individuals who know that they will have to justify their actions are more likely to consider the social consequences of their decisions and to take others’ interests into account (Lerner & Tetlock, 1999; Tetlock, 1992). For example, US Presidents exhibit greater cognitive complexity after having been elected, when they become accountable to a variety of constituents, than before election (Tetlock, 1981).

5. CONCLUSIONS

Mergers and acquisitions are big business: 29,312 firms were merged or acquired in 2008, at a cost of $2.56 trillion to the shareholder (Wilmerhale, 2009). Mergers should allow the firm to cut-costs, and/or expand revenues (Besanko et al., 2006), and as such are critical for the firm seeking to increase its global reach and competitiveness (Lasserre, 2006). The “overwhelming majority” of studies, however, find that they “do not positively contribute to [...] performance” (King et al. 2004). And estimates suggest that as many as 65 to 85% fail (Puranam & Singh, 1999).

The extant literature adopts a predominately finance-orientated perspective in attempting to understand success and failure, and assumes that mergers and acquisitions are a ‘closed system’, with little room for human interference; in spite of the fact that estimates suggest that the manager may be responsible for between one third to one half of all merger failures (Cartwright & Cooper, 1990; Dannemiller Tyson, 2000). In this research we suggest that managerial power is thus a long neglected moderator of merger performance, because managers have a unique opportunity to create or destroy value in the merger process. Consequently, we adopt a multidisciplinary perspective, which puts the manager under the microscope.

In the process, we show that the managers ‘experience of power’ causes overconfidence, results in risk-taking behavior, and may lead the manager to believe the old – and defunct – adage that a ‘good manager can manage anything’. At the pre-merger stages, this results in value-destruction, because mergers may be unnecessarily pursued, and targets sought out and approved, on the basis of fuzzy and subjective concepts, such as ‘instinct’ and ‘gut feeling’, rather than rigorous economic analysis.

Right or wrong, our findings suggest that the manager’s experience of power may facilitate the negotiation and bargaining processes during which the merger is agreed, and may increase the probability that value will be created. Powerful
managers, we suggest, are also better able to communicate the grander goals of the merger, and their lack of emotional empathy will aid in the objectivity with which they restructure the organization, and ‘cut the dead wood’ to realize synergies.

We suggest, however, that a general disinterest in the detail, and an inability to communicate the day-to-day details of the integration plan, will typically result in value-destruction. Powerful managers, we suggest, will simply not invest in the ‘nitty-gritty’ of integration planning, and will prefer instead to take a ‘hands on approach’. Furthermore, and in the evaluation stage, we suggest that powerful managers are less likely to be harsh on themselves, and will consider ‘failures’ as mere ‘set-backs’.

To ensure that value is created, we thus argue that an awareness of the role of managerial power is necessary. And claim that to manage the M&A process, the managers – that is, the person in a position of power – needs to be managed. We suggest that by understanding the systematic effects of power on the thought processes and behaviors of managers, the constructive forces bestowed upon the manager by power – in negotiations and restructuring, for example – can be harnessed, while it’s more dysfunctional effects on performance can be mitigated. In doing so, we hope to contribute both to scholars and practitioners in the field. And demonstrate that the boundaries of the firm can be altered, but only with due care.

REFERENCES


Chatterjee, S., (1986), Types of Synergy and Economic Value: The Impact of Acquisitions on Merging and Rival Firms, Strategic Management Journal Vol. 7 (Mar – Apr., 1986), 119-139


