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Source: *Strategic Management Journal*, Jul. - Aug., 1989, Vol. 10, No. 4 (Jul. - Aug., 1989), pp. 307-322

Published by: Wiley

Stable URL: https://www.jstor.org/stable/2486459

Strategic Management Journal, Vol. 10, 307–322 (1989)

DOING A DEAL: MERGER AND ACQUISITION NEGOTIATIONS AND THEIR IMPACT UPON TARGET COMPANY TOP MANAGEMENT TURNOVER

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This research investigates the effects of merger and acquisition negotiations on subsequent target company top management turnover. Three attributes of the companies and seven attributes of the merger and acquisition transactions are examined. The results indicate that the primary impact of negotiations is evident in the fourth year after a settlement date. When a buyer approaches an unrelated company that has been subject to previous takeover interest with a merger proposal, and an agreement is reached, the target's management team is likely to experience abnormally high turnover 4 years later. Additional research ideas are suggested to help explain the sizeable turnover rates in the 3 years immediately following a merger or acquisition.

A total of 71,893 merger and acquisition announcements were made between 1963 and 1986 (W. T. Grimm & Company, 1987). Despite the prevalence of such activity, our understanding of mergers and acquisitions is surprisingly limited. Jemison and Sitkin (1986) argued that we should examine such activity from three perspectives and assess the strategic fit, the organizational fit, and the merger and acquisition process itself.

To date, the study of strategic fit and synergy has been most prominent in the literature (Chatterjee, 1986; Lubatkin, 1983; Rappaport, 1979; Rumelt, 1974; Salter and Weinhold, 1979). A concern about strategic fit has spawned a tremendous interest in the financial implications of mergers and acquisitions (Halpern, 1983; Jensen and Ruback, 1983; Mueller, 1977). While this merger and acquisition activity has been noticed in the organizational sciences, it has not particularly captured the research attention of the field. At the moment our understanding of organizational fit has come primarily from a few well-documented case studies (Blumberg and Wiener, 1971; Buono, Bowditch and Lewis, 1985; Costello, Kubis and Shaffer, 1963; Graves, 1981; Mirvis, 1985; Sales and Mirvis, 1984). Finally, our understanding of how pre-merger and acquisition events can help or hinder merger and acquisition success is very limited. Nevertheless, Jemison and Sitkin (1986: 148) argued that 'the acquisition process itself (the courtship) may be related to the ability to make the business combination (the marriage) successful'.

This 'courtship' may be viewed as a process of negotiation. Rubin and Brown (1975: 2) defined negotiation as a 'process whereby two or more parties attempted to settle what each shall give and take, or perform and receive, in a transaction between them'. Therefore, an understanding of merger and acquisition negotiations must include, at minimum, an understanding of the *parties* themselves and the *transaction* that ensues between them (Lewicki and Litterer, 1985; Morley and Stephenson, 1977; Pruitt, 1981; Rubin and Brown, 1975). As such, this investigation of merger and acquisition negotiations will examine both the attributes of the two companies involved and their transactions prior to the settlement date.

The present examination of merger and acquisition negotiations responds to Hayes' (1979) thought that such negotiations should affect the retention of the acquired company's top management. He argued that 'professional negotiations' should be associated with top management retention (p. 42). This investigation also responds

0143–2095/89/040307–16$08.00

Received 18 April 1988
Final revision received 10 October 1988

to Walsh's (1988) call for such research following his inability to account for top management turnover across target companies using the relatedness of the merger or acquisition as a predictor.

The importance of target company top management turnover is apparent from many perspectives. Top managers themselves are very concerned about the impact of mergers and acquisitions on their own lives (Bennett, 1986; Prokesch, 1985). Hirsch (1986: 825) observed that this impact has been pervasive; it was initially viewed 'as the managerial equivalent of a natural disaster'. He argued that as the language that frames takeovers changed over the years, it served to legitimate their occurrence and maybe even ease the personal disruptions that may follow takeovers. As a result, the term 'wounded list' emerged to identify the 'executives of an acquired firm who develop health or career problems from the deal' (p. 835). While we have now come to expect executives to be 'wounded' from deals, we do not know which deals place them at the greatest risk. Our understanding of how these 'wounds' are inflicted is limited. Management scholars are interested in the phenomenon as a part of their quest to understand post-merger integration processes (Drucker, 1981; Parsons and Baumgartner, 1970; Pitts, 1976; Walsh, 1988). They wonder if such turnover helps or hinders future organizational performance. Finally, those who view mergers and acquisitions as a reflection of a market for corporate control seek to understand target company top management turnover because it is a key measure of the outcome of the competition among companies to determine the right to manage a target company's resources (Easterbrook and Fischel, 1981; Fama and Jensen, 1983; Jensen and Ruback, 1983; Manne, 1965). Indeed, as one justification for his corporate raiding, T. Boone Pickens argues that he is trying to hold America's top executives accountable for their sometimes lackluster performance (Pickens, 1986).

The purpose of the present research is to investigate how the merger and acquisition negotiations affect the retention of a target company's top management. Following Rubin and Brown (1975), this research examines how attributes of the two companies, and the attributes of the transaction itself, affect the turnover of a target company's top management team for as many as 5 years after the consummation of a deal. The hypothesized effects and their rationale are presented below.

MERGER AND ACQUISITION NEGOTIATIONS AND TOP MANAGEMENT TURNOVER

It is well known that the nature of a negotiation between two parties affects their subsequent relationship. In Fisher and Ury's (1981: 7) words, a contentious negotiation can 'strain and shatter' a relationship. In a merger and acquisition context these negotiations may affect the willingness and ability of the top management teams to work together in the new business combination. Indeed, the negotiations surrounding the recent wave of mergers and acquisitions have captured the attention of the popular business press (Johnson 1986; Taylor, 1987). We know that top management turnover following a merger or acquisition is higher than 'normal' (Walsh, 1988). We also know that some negotiations are fueled by a rationale which establishes an intent to rid an undervalued acquisition target company of the incompetents who have presumably mismanaged it (Law, 1986). Nevertheless, some negotiations can be quite friendly, marked by a noticeable absence of such rhetoric. We do not know, however, if these different negotiations are systematically related to differential top management turnover rates. The intent of this research is to begin to answer Jemison and Sitkin's (1986) call to understand the merger and acquisition process by examining the relationship between merger and acquisition negotiations and subsequent top management turnover. A number of attributes of the companies and their transaction will be investigated.

Attributes of the companies

Three attributes of the companies and their interrelationships will be examined. Specifically, the type of merger or acquisition, the size difference between the parent and target, and any previous interest in the acquisition of the target company are hypothesized to affect a target company's top management turnover rate.

Walsh's (1988) hypothesis that top management turnover following a related merger or acquisition would be higher than the turnover following an unrelated merger or acquisition will be re-examined in this investigation. While his analysis of 50 mergers and acquisitions did not support this hypothesis, the means were in the predicted direction. He argued that the parent company's management team is familiar with a target company's business in a related merger or acquisition. As such, the parent can afford to lose many of the target company's managers. Indeed, Manne (1965) suggested that they may even encourage their departure. In an unrelated merger or acquisition, however, the parent company might be more dependent upon the target's managers and thus they should be interested in retaining them. In fact, Pitts (1976) argued that, in such cases, the acquiring firm cannot afford to lose the product and market experience of the target company's management. This hypothesis will be re-examined with this investigation's broader sample of mergers and acquisitions. Accordingly:

> *H1: A target company's top management turnover rate is likely to be higher following a related merger or acquisition than following an unrelated merger or acquisition.*

The size difference between a parent company and target company should affect top management turnover. That is, a very large company is likely to have a supply of skilled managers on hand to replace the managers in a smaller acquired company. This would not be the case as the size difference between the parent and target diminishes. Moreover, the managers in the smaller target company may be less skillful when managing in a larger and perhaps more bureaucratic context. As such:

> *H2: Target company top management turnover rates are likely to vary positively with an increase in the size difference between the parent and target companies.*

Finally, target companies vary in the level of interest that they may have received from other buyers before the current deal was accepted. Bradley, Desai and Kim (1983) found that pre-announcement abnormal returns persisted for up to 2 years after an unsuccessful takeover attempt for those firms that were eventually acquired. Such abnormal returns vanished for those firms that received no subsequent offers. This would indicate that the market may recognize truly undervalued or inefficient companies. Following a market for corporate control logic, if past buyers have recognized an inefficient management team, and expressed some interest in buying the target, and that target is eventually purchased, it is likely that the turnover rate among those managers will be higher than the turnover rate in a target company that has not been subject to previous merger and acquisition interest. Jensen (1987) might argue that the resistance in such cases would be motivated only by the top managers' parochial self-interests. Therefore:

> *H3: A target company's top management turnover rate is likely to be higher when that company has been subject to, rather than free from, previous merger and acquisition interest.*

Attributes of the transaction

Seven attributes of the transaction will be investigated in this research. The approach of the acquirer (i.e. merger or tender offer), the nature of the bargaining (i.e. number of counter-offers and the number of days to settlement), explicit talk of management retention, the press characterization of the nature of the transaction (i.e. friendly, neutral, or hostile), the nature of payment (i.e. cash, stock, or a combination), and the premium paid for the company are all hypothesized to affect top management turnover.

The parent may decide that it cannot work with the target company's managers to effect the transaction. Often in such circumstances, it will attempt to purchase the company by way of a direct tender offer to the shareholders. In such instances, it is unlikely that the parent company will retain the target's top managers if the tender offer is accepted. Similarly, target company managers are likely to be displeased if a parent company bypasses them and makes a direct offer to the target company's shareholders. They are unlikely to want to continue working for the new parent company after the two companies have been combined. Accordingly:

> *H4: A target company's top management turnover rate is likely to be higher following a tender offer than a merger.*

Proponents of principled bargaining (Fisher and Ury, 1981) argue that parties to a negotiation should focus on each other's interests and offer a single price that is based fairly on objective criteria. In this way the parties avoid what Fisher and Ury (1981: 6) called the 'standard minuet' — that is, 'starting with an extreme position, stubbornly holding onto it, deceiving the other party as to your true views, and making small concession only as necessary to keep the negotiation going'. This 'standard minuet' or positional bargaining style is what can 'strain and sometimes shatter the relationship between the parties' (p. 7). Merger and acquisition negotiations characterized by such positional bargaining are likely to strain and shatter the relationships between the top management teams, resulting in high top management turnover in the target company. Two measures of positional bargaining will be assessed in this research. The number of counter-offers made by the buyer will be seen as evidence of positional bargaining, as will a protracted period of negotiation. As such:

H5: A target company's top management turnover rate is likely to be higher following a negotiation marked by a number of counter-offers being made for the company.

H6: Target company management turnover rates are likely to vary positively with the amount of time required to negotiate a deal.

Occasionally, the buyer issues a public statement during the course of the merger or acquisition negotiations assuring the managers of the target company that they will retain their jobs following an agreement. Acknowledging Gaddis' (1987: 16) admonition that 'pre-merger discussions bring no guarantees', this assurance will be taken at face value for the purpose of this research. It is expected that top management turnover rates will reflect the presence of such statements. Therefore:

H7: A target company's top management turnover rate is likely to be lower following a buyer's public assurance of top management retention than when the buyer issues no such guarantees.

During the course of a negotiation, the press characterizes the negotiations as friendly, neutral, or hostile. Top managers that express open hostility with the prospect of a merger or acquisition are unlikely to remain in the target company following an agreement. Accordingly:

H8: A target company's top management turnover rate is likely to be higher following hostile, rather than friendly, merger or acquisition negotiations.

Top management turnover is likely to vary with the method of payment for the target company (i.e. stock, cash, a combination of stock and cash). Hansen (1987) argued that a target company will prefer a stock transaction when it knows that its assets are of high value. That is, the target anticipates that the stock it receives for the transaction will increase in value as it subsequently makes a positive contribution to the value of the merged entity. A perception of a high-quality management team may contribute to the high valuation of these assets. As a result, we would expect lower top management turnover rates following a stock deal. In contrast, the target has an incentive to accept a cash offer only if it knows that its value is less than the value of the cash offer. A target's recognition of its own poor-quality management team may contribute to this sense of a lower value. When the parent discovers that the target's value is not what it expected, the target's top managers are likely to turn over. As such:

H9: A target company's top management turnover rate is likely to be lower following a merger or acquisition paid for in stock, rather than a combination of stock and cash, or cash alone.

Typically, a buyer pays some premium over the average market value of the target company's stock. This can vary from a few percentage points to more than two or three times the target company's 'normal' value. If a parent pays a high premium for a target company it must recognize that the target is very undervalued. The parent's attribution for such a discrepancy is often that the target's top managers are ineffective or incompetent (see Johnson's, 1986, discussion of takeovers in the oil industry). In such cases subsequent management turnover is likely to be high. Indeed, Oviatt (1988) made this same point recently. Moreover the payment of a high premium to managers (who typically have some equity in the company) might be a way of 'buying-out' entrenched managers. Therefore:

> *H10: A target company's top management turnover rate is likely to vary positively with the premium paid for the target company.*

Each of these ten hypotheses predicts the magnitude of top management turnover. It is uncertain, however, when this turnover is likely to occur. With this in mind, target company top management turnover will be assessed at each of 5 years after the settlement date. This aspect of the research effort is exploratory.

METHODS

Sample

A sample of merged and acquired companies was drawn from the *Statistical Report on Mergers and Acquisitions, 1979* (1981). This report was published each year by the Federal Trade Commission, ending with the publication of the 1979 data in 1981. The report lists all manufacturing and mining companies with assets of at least $10 million that were merged with or acquired by publicly held U.S. companies. Mergers and acquisitions are categorized into a five-fold typology: horizontal, vertical, product extension, market extension, and unrelated conglomerate. The exact date of each acquisition is listed as well.

Walsh (1988) surveyed 130 parent companies that had merged with or acquired a company between the years 1975 and 1979. He sampled all of the vertical and market extension acquisitions of that time period and sampled randomly from the other three categories. This effort yielded data on target company top management turnover rates for 55 companies, with complete data for 50 companies.

Walsh's (1988) survey data are employed again in this research; however, they have been augmented by a second data collection effort. One hundred and ten additional parent companies were randomly selected and surveyed from among the lists of horizontal, product extension, and unrelated conglomerate mergers and acquisitions of this same time period. Fifty-eight usable responses were received, although six companies sent incomplete information; six companies responded with an apology because they could not provide us with the information requested; 46 companies did not respond at all to the initial and follow-up requests. Including Walsh's (1988) data, 240 parent companies were contacted to create the current data base. Usable responses were received from 113 companies, although complete top management turnover data are available for only 102 companies. This response rate of 47 percent is much higher than the 20 percent mailed survey response rate predicted by Gaedeke and Tootelian (1976). The final sample is composed of 20 horizontal, 11 vertical, 36 product extension, 5 market extension, and 41 unrelated conglomerate mergers and acquisitions.

Procedure

Members of the 240 target companies' top management teams at the time of the merger or acquisition were identified by examining each company's 10-K or annual report. After identifying each executive by name, age and position, a survey was prepared. A call to each parent company identified a human resources officer to whom we could mail the survey. The survey listed each member of the target's top management team at the time of the merger. It asked the human resources officer in the parent company to examine their personnel records and report the subsequent career histories for each executive. The parent company representative was asked to identify whether or not each executive was still employed by what was the target company. If the executive had left the target company, the representative was asked to provide the date of departure.

Measures of the merger and acquisition negotiation process variables for all the companies that responded to the survey were created by coding every *Wall Street Journal* article written about the events leading to each of the mergers and acquisitions captured in our sample. Every article, from the first hint of a possible merger or acquisition, until the formal announcement of a deal, was read and coded for evidence of each of the variables of interest not accounted for in the FTC publication. Given that the coding of the variables investigated in this research is an unambiguous task, one person did all of the coding.

Operationalizations

Target company top management turnover

The name of each member of the target company's top management team at the time of the merger or acquisition was identified in its 10-K or annual report. The mean number of executives that comprised the top management team was 8.19, with a standard deviation of 3.49. They held such titles as 'Chairman of the Board', 'President', 'Executive Vice-President', 'Senior Vice-President', 'Treasurer', and the like. With the date of departure information provided by the survey responses, we were able to compute the cumulative percentage of the top management team that turned over at each of 5 years after the date of the merger or acquisition. The differences between the cumulative yearly percentages yielded measures of annual turnover rates for each year of observation.

Type of merger or acquisition

As noted above, the Federal Trade Commission created a five-fold category system for the classification of mergers and acquisitions. Horizontal, vertical, product extension, and market extension mergers and acquisitions are all coded as related in this research. Unrelated conglomerate mergers and acquisitions are coded as unrelated. The sample is composed of 64 percent related and 36 percent unrelated mergers and acquisitions.

Asset size differences

The mean asset size of the sample of parent companies is \$1.382 billion with a standard deviation of \$1.985 billion (the range is \$14 million to \$11.187 billion); while the mean target company asset size is \$87.602 million with a standard deviation of \$137.140 million (the range is \$10 million to \$764 million). Due to the sizeable variance in assets, the logarithms (base 10) of both the parents' and targets' assets were computed. The difference between the logarithm of the parent's assets and the target's assets at the time of the merger or acquisition established the asset size difference between the two companies. The mean difference was 1.084 with a standard deviation of 0.727 (the range is −0.33 to 2.97).

Previous merger and aquisition interest

If any mention was made in the *Wall Street Journal* during the course of the merger or acquisition negotiations that the target company had received previous takeover interest from another company, it was recorded. Twenty-three percent of the sample was found to have been subject to such interest. Note that this variable does not imply that the current parent is a 'white knight'. The coding of this variable simply indicates that the target company had received other takeover interest prior to its subsequent purchase by the parent.

Acquirer's approach

Wall Street Journal articles were coded to portray whether the buyer approached the target's managers with a merger proposal or bypassed these managers and approached the target's shareholders directly with a tender offer. The sample is composed of 63 percent mergers and 37 percent tender offers.

Number of offers

The *Wall Street Journal* recorded the progress of the merger and acquisition negotiations. In 78 percent of the cases the buyer made one offer for the target company, and it was accepted. In 22 percent of the negotiations captured in this sample the future parent company was forced to make one or more counter-offers before the final price was agreed upon.

Days to settlement

For each merger and acquisition the number of days was recorded between the time the names of the buyer and the target company were first linked in the *Wall Street Journal*, and the time the formal agreement of the merger or acquisition was established. The mean number of days to settlement was 116.91 with a standard deviation of 99.74 days. Note that this measure captures the time frame in which the negotiations were public knowledge. There is no way of knowing how long the negotiations may have taken place in private.

Assurance of management retention

In 81 percent of the merger and acquisition negotiations the buyer made no mention in the *Wall Street Journal* of retaining the target company's managers. However, in 19 percent of the negotiations the future parent company did make such assurances.

Press characterization

In many mergers and acquisitions the press will reveal whether the negotiations are friendly or hostile. In this research the negotations were coded as friendly, neutral, or hostile based upon the characterization of the negotiations in the *Wall Street Journal*. Friendly negotiations were either explicitly labeled as such or they were reported as unambiguously positive (e.g. 'Company F said it would urge its shareholders to accept the offer'). Neutral negotiations were seen as neither friendly nor hostile. The following quotation captures a typical neutral negotiation: 'Company N expects the talks to continue; however, the company declined to elaborate'. Finally, hostile negotiations were either coded from a direct reference to hostility in the press or from unambiguously negative comments (e.g. 'The chairman of the board of Company H vigorously opposed the offer. "It is totally inadequate," he said, "it is a rush Saturday-night special"'). In all, the sample is composed of 42 percent friendly, 46 percent neutral, and 12 percent hostile merger and acquisition negotiations.

Method of payment

The method of payment was reported in the *Statistical Report on Mergers and Acquisition, 1979* (1981) for each of the mergers and acquisitions. Fifty-three percent of the companies were paid for in cash; 35 percent were paid for in stock; and the remaining 12 percent were paid for in a combination of cash and stock.

Premium paid

The target company's stock price was compiled for each day in the fourth week prior to the buyer's first public interest in the target company. This date is the first day in the 'days to settlement' variable. The mean of these five observations was computed and divided by the final settlement price of the target company's stock. In all cases the premium paid was positive. It ranged from 0.19 percent to 493.14 percent, with a mean of 62.37 percent and a standard deviation of 60.28 percent.

It should be noted that empirical studies of movement in the stock prices of target firms consistently show evidence of abnormal returns prior to the announcement date of a transaction (Jensen and Ruback, 1983). However, these studies indicate that the abnormal effects do not begin to appear until 30 days before the announcement date (Asquith, 1983; Bradley, 1980; Dodd, 1980). By sampling target company stock prices 4 weeks before its name was first linked with the parent company in the press, we avoided this abnormal effect in the calculation of the premium paid by the buyer. Recall that, on average, the settlement date is 116.91 days away from the day the two company's names are first linked in the press.

RESULTS

We could not predict when the effects of the hypotheses would be evident. Table 1 profiles the *cumulative* mean target company top management turnover rates in the entire sample and by each of the ten variables of interest. The turnover is recorded at each of 5 years after the consummation of the deal. Although three of the ten variables are continuous, a categorical variable was created in each case (by a median split) to give the reader a sense of the magnitude of the turnover associated with those variables (e.g. asset size difference, days to settlement, and premium paid). The magnitude of top management turnover across all 102 target companies is sizeable. The management team turnover rate is 26.07 percent after the first year; it increases to 61.13 percent by the time the target company has been with the parent company for 5 years. The annual increase in top management turnover

Table 1. Cumulative mean target company top management turnover rates by the merger and acquisition negotiation variables

	Years after a Merger or Acquisition				
	1	2	3	4	5
Type of merger or acquisition					
Related	29.95	39.64	51.09	55.29	62.09
Unrelated	23.33	39.17	46.83	57.27	63.17
Asset size difference					
Greater than median (0.986)	26.80	40.11	50.48	56.73	64.75
Less than median (0.986)	28.49	38.78	48.63	55.20	60.02
Previous takeover interest					
Yes	19.95	30.81	47.33	59.48	64.67
No	30.13	42.31	50.33	54.84	61.75
Acquirer's approach					
Merger	30.63	40.37	49.54	56.37	62.86
Tender offer	21.46	37.64	49.68	55.21	61.68
Number of offers					
One	27.30	38.39	48.82	55.25	61.94
Two or more	28.78	43.50	52.44	58.72	64.44
Days to settlement					
Greater than median (93 days)	32.63	40.47	52.44	58.73	63.19
Less than median (93 days)	22.48	38.45	46.67	53.55	61.74
Assurance of retention					
No	26.06	38.24	48.46	55.16	61.13
Yes	33.39	44.06	53.78	59.06	67.44
Press characterization					
Friendly	24.49	35.51	48.05	55.44	62.15
Neutral	27.26	40.47	48.58	53.55	60.29
Hostile	44.50	54.00	61.88	70.25	74.38
Method of payment					
Stock	29.03	36.60	47.80	56.53	63.77
Cash and stock	28.50	39.33	49.67	56.75	62.00
Cash	26.37	41.65	50.81	55.40	61.70
Premium Paid					
Greater than median (50.68%)	29.86	39.91	48.55	55.48	60.36
Less than median (50.68%)	25.20	39.00	50.71	56.54	64.73
Total sample (n=102)					
Mean	26.07	38.60	48.85	54.92	61.13

Note: All statistics are expressed as percentages.

begins with 26.07 percent in the first year and continues with increases of 12.53, 10.26, 6.07, and 6.21 percent in each of the next 4 years.

Table 2 presents the correlations among the ten predictor variables and the five measures of top management turnover. Pearson product–moment and phi coefficients are reported as appropriate. Only the *annual* increases in turnover are examined. The obviously high intercorrelations among the cumulative measures of target company turnover compromise their meaningful use in the statistical analyses. Interestingly, the correlations among the five measures of turnover indicate that early top management turnover in a target company is likely to occur predominantly in a single year. The correlation between the first year turnover rate and the second year rate is -0.30 ($p<0.001$); the correlation with the third year rate is -0.28 ($p<0.01$). Moreover, the correlation between the second year and the third year turnover rate is -0.18 ($p<0.05$). The absence of any positive correlations between early and later turnover indicates that there is no evidence of any subsequent compensatory turnover that might be thought to 'correct' for these early negative autocorrelations.

Table 2. Correlations among the variables

		A	B	C	D	E	F	G	H	I	J	K	L	M	N	O
M & A Type	A	—														
Size difference	B	−0.09	—													
Previous interest	C	0.01	0.23***	—												
Acquirer's approach	D	0.20**	−0.27***	0.43****	—											
Number of offers	E	0.18**	0.05	0.24***	0.23***	—										
Days to settlement	F	−0.05	−0.01	−0.09	−0.05	0.20**	—									
Assurance of retention	G	−0.04	−0.14*	0.12	0.01	−0.09	0.05	—								
Press characterization	H	0.02	0.03	0.02	0.15*	0.37****	0.10	−0.09	—							
Method of payment	I	0.20**	−0.07	0.20**	0.59****	0.18**	−0.07	0.00	0.02	—						
Premium paid	J	−0.03	−0.08	0.16**	0.01	0.03	−0.04	−0.04	−0.01	−0.06	—					
Fifth year turnover	K	−0.05	0.10	−0.10	−0.01	−0.05	−0.09	0.08	−0.06	−0.04	−0.15*	—				
Fourth year turnover	L	0.21**	−0.09	0.28***	−0.05	−0.00	−0.07	−0.07	−0.04	−0.20**	−0.03	−0.02	—			
Third year turnover	M	−0.01	−0.04	0.19**	0.07	−0.06	0.02	−0.02	−0.13	−0.10	−0.01	0.01	−0.08	—		
Second year turnover	N	0.10	0.16*	−0.07	0.15*	0.03	−0.16*	0.02	0.03	0.18**	−0.18**	−0.07	−0.03	−0.18**	—	
First year turnover	O	−0.04	−0.02	−0.05	−0.13	0.05	0.07	0.12	0.19**	0.02	−0.02	−0.24***	−0.10	−0.28***	−0.30****	—

Note: M & A Type (1=Related; 2=Unrelated), Previous interest (1=No; 2=Yes), Acquirer's aproach (1=Merger; 2=Tender offer), Number of offers(1=One; 2=More than one), Assurance of retention (1=No; 2=Yes), Press characterization (1=Friendly; 2=Neutral; 3=Hostile), Method of payment (1=Stock; 2=Stock and Cash; 3=Cash).

* $p<0.10$; ** $p<0.05$; *** $p<0.01$; **** $p<0.001$.

The intercorrelation matrix provides a good deal of descriptive evidence about the nature of merger and acquisition negotiations. The previous history of the target company in the market is associated with a number of company and transaction attributes. A target company that has been subject to takeover interest before it is ultimately purchased, is likely to be purchased by an unrelated company (r=0.20, p<0.05) of similar asset size (r=−0.27, p<0.01). The buyer is likely to have made a number of offers for the target company (r=0.24, p<0.01), eventually paying a high premium (r=0.16, p<0.05) in cash (r=0.20, p<0.05). The future parent is likely to approach such a company with a tender offer (r=0.43, p<0.001).

Given these correlations, it is no surprise to discover that tender offers are associated with the unrelated acquisition (r=0.20, p<0.05) of companies of similar asset size (r=−0.27, p<0.01). Typically, tender offers are paid for in cash (r=0.59, p<0.001) after at least one counter-offer is made (r=0.23, p<0.01). The press characterizes such negotiations as hostile (r=0.15, p<0.10). In fact, the press often portrays negotations involving one or more counter-offers as hostile (r=0.37, p<0.001).

By focusing explicitly on the number of counter-offers as a measure of positional bargaining, we discover that these negotiations are likely to involve two unrelated companies (r=0.18, p<0.05), where the target has been subject to previous takeover interest (r=0.24, p<0.01). In such cases the buyer seems to approach the target with a tender offer (r=0.23, p<0.01). After a protracted period of negotiation (r=0.20, p<0.05), the two companies tend to agree on a cash settlement (r=0.18, p<0.05).

This descriptive portrait of the merger and acquisition negotiations provides a context to examine their effects on the turnover of top managers in the target company. While the ten hypotheses predict effects of company and transaction attributes on top management turnover, the time period in which this turnover is expected to occur was not predicted. Accordingly, the bivariate correlational relationships between each of the predictors and the five measures of yearly top management turnover are examined.

Three attributes of the two companies and their relationships were hypothesized to be related to subsequent target company top management turnover. There is no correlational support for H1 in these data. In fact, the results indicate that top management turnover in the fourth year after a deal is *higher* following unrelated, rather than related, mergers and acquisitions (r=0.21, p<0.05). The correlation of 0.16 (p<0.10) between the turnover in the second year and increasing parent–target asset size differences is consistent with H2. Finally, the positive correlations between previous takeover interest in a target company and that company's subsequent top management turnover rate in years three (r=0.19, p<0.05) and four (r=0.28, p<0.01) are consistent with the logic of H3.

Seven aspects of the negotiations that lead to an agreement were predicted to be associated with top management turnover. These relationships are reflected in hypotheses four through ten. As predicted in H4, the correlational results suggest that tender offers, relative to merger agreements, are associated with higher management turnover. This relationship shows up in second year turnover rate (r=0.15, p<0.10). H5 received no support with these data. No relationships between the number of counter-offers and turnover are revealed here. The logic of H6 was challenged in the correlation of −0.16 (p<0.10) between the amount of time the negotiations took and turnover in the second year. Deals consummated fairly quickly seem to be associated with higher turnover, not lower turnover. There was no support for H7 in these results. A buyer's assurance that the top managers will keep their jobs is not related to subsequent turnover at all!

As predicted in H8, a target company's managers seem to turn over at a higher rate following hostile, rather than friendly, negotiations. The correlation between hostility and such turnover is significant in the first year after the merger or acquisition agreement is reached (r=0.19, p<0.05). The relationships between the various methods of payment and turnover are interesting. Consistent with H9, the turnover in the second year is higher following a cash payment (r=0.18, p<0.05). However, with time, the relationship changes. In the fourth year, managers employed by target companies paid for in stock are likely to turn over (r=−0.20, p<0.05).

It may be that part of a premium paid for a target company is the quality of its management.

The inverse of the logic of H10 was supported with the negative correlations between the amount of premium paid for a company and the turnover rates in the second year ($r=-0.18$, $p<0.05$) and in the fifth year ($r=-0.15$, $p<0.10$).

Finally, a series of analyses of covariance (ANCOVA) that entered the covariates and factors simultaneously were run to examine the effects of the seven categorical variables as main effects and the three continuous variables as covariates on the five measures of top management turnover. Only the ANCOVA that predicted the top management turnover in the fourth year after a merger or acquisition reached statistical significance. As Table 3 indicates, the explained variance [$F(12,72)=3.67$)] was significant at the 0.001 level in this ANCOVA. Specifically, the top management turnover rate among the target's original managers in the fourth year is higher among mergers ($M=6.82$ percent) than tender offers ($M=5.54$ percent), $F(1,72)=7.13$, $p=0.009$. Managers in target companies that were subject to previous merger and acquisition interest ($M=12.14$ percent) turned over at a significantly higher rate than those who were not employed by such target companies ($M=4.52$ percent), $F(1,722)=22.78$, $p=0.000$. Finally, top managers employed by unrelated target companies ($M=10.43$ percent) turned over at a significantly higher rate than their peers in related target companies ($M=4.20$ percent), $F(1,72)=13.82$, $p=0.000$. In summary, H3 received support from the ANCOVA, while the inverse of the predictions of H1 and H4 were supported. This H4 result is interesting in light of the correlational support it received. It would seem that H4 (along with H9) might be time-dependent.

DISCUSSION

These results support Walsh's (1988) finding that there is widespread target company top management turnover following mergers and acquisitions. The cumulative turnover rates in each of 5 years after a merger or acquisition are 26, 39, 49, 55, and 61 percent, respectively. These rates are much higher than the 'normal' top management turnover in companies of similar size to the target companies examined here. Walsh (1988) found that the comparative rates are 2, 13, 21, 31, and 33 percent. While Drucker's (1981) fear of wholesale top management turnover in the first year seems to be misplaced, the evidence still suggests that many top executives are at risk of being 'wounded' (Hirsch, 1986) by merger and acquisition activity. The intent of the present research has been to try to understand the origins of this turnover.

Building upon the logic of Hayes (1979), Jemison and Sitkin (1986) and Walsh (1988), the natures of the merger and acquisition negotations were predicted to covary with the magnitude of top management turnover. Following Rubin and Brown (1975), the attributes of the two companies

Table 3. Results of the analysis of covariance for the target company top management turnover in the fourth year by the merger and acquisition negotiation variables

Source of variation	Sum of squares	Degrees of freedom	F	Significance of F
Days to settlement	141.86	1	1.70	0.196
Premium paid	21.45	1	0.26	0.614
Asset size difference	19.25	1	0.23	0.632
Acquirer's approach	594.84	1	7.13	0.009
Press characterization	285.88	2	1.71	0.188
Number of offers	140.91	1	1.69	0.198
Method of payment	311.85	2	1.87	0.162
Assurance of retention	192.76	1	2.31	0.133
Previous M&A interest	1900.33	1	22.78	0.000
M&A type	1153.25	1	13.82	0.000
Explained	3674.10	12	3.67	0.000
Residual	6006.30	72		
Total	9680.40	84		

and the transactions that ensued between them were assessed. The most striking finding of this investigation was that *only* the ANCOVA predicting the fourth year turnover rate was statistically significant. This is particularly important in light of Walsh's (1988) finding that the differences in the turnover rates between merged and non-merged companies are set in the first year after a merger. Beyond this first year the rates of increase are the same. The negative correlations between the first year rate and the second and third year rates bear added testimony to the importance of understanding this early post-merger turnover. Unfortunately, only the absence of many early effects of the negotiations on management turnover is illuminating in this instance. The timing of both the present effects and the absent effects in this research needs to be better understood.

The case study evidence indicates that the period after a merger or acquisition is marked by great uncertainty and upheaval in the target company especially (Buono, Bowditch and Lewis, 1985; Mirvis, 1985; Sales and Mirvis, 1984). This uncertainty and upheaval tests the management capabilities of those charged with integrating the new business combination (Shrallow, 1985; Shrivastava, 1986). Given that the parent company must be poised to handle a nearly 50 percent loss of the target's top managers as a normal consequence of the activity in the 3 years after a merger (Walsh, 1988), it seems that both the parent and the target company managers are reluctant to let their negotiation experience compound the already serious problems of post-merger integration. This may explain the absence of effects for the early years after a new organizational combination. After all, these are $88 million dollar companies that need to be managed. Most likely, some management continuity is needed to facilitate the continued operation of the target company. Indeed, Tables 1 and 2 reveal that only the hostility of the negotiations was associated with the sizeable first year turnover. Perhaps emotion is ruling reason in these instances? It would be interesting to learn if the post-acquisition integration process was helped or hindered by the high early turnover following each hostile negotiations.

As evidenced by the hostility effect, the bivariate correlational results offer a few glimpses of what might be happening in this early post merger period. The two measures of a positional bargaining style (e.g. number of offers and days to settlement) did not predict management turnover as expected. Indeed, even though the number of offers was correlated with a measure of hostility, it was completely unrelated to top management turnover. The surprisingly negative correlation between days to settlement and second year turnover suggests that a protracted amount of time spent in pre-acquisition negotiations may reflect the kinds of pre-acquisition integration planning that have been advocated (Fray, Gaylin and Down, 1984; Perry, 1986), rather than contentious bickering.

A second surprise to emerge from these results is the negative correlations between the premium paid for the company and the second and fifth year turnover rates. These findings suggest that an incompetent, entrenched management team might not be commonly associated with an undervalued firm. In contrast to the logic of those who view merger activity as a check on poorly performing managers, it could be that acquiring companies are buying good managers with their high premiums rather than buying-out poor ones.

A third, and perhaps not surprising, result to emerge from Table 2 is the absence of a statistically significant relationship between a parent company's assurance that the target company managers will retain their jobs and the empirical evidence of such assurances. Gaddis (1987) after all did warn us to be skeptical of pre-merger discussions. Just the same, the directions of the means might give some managers pause. The turnover rate among those whose jobs were guaranteed in the pre-merger period was on average (across the 5 years) 5.74 percent *higher* than their colleagues who received no such assurances!

The major effects to emerge in this research are reflected in the ANCOVA Results. These ANCOVA results indicate that when a buyer approaches an unrelated company that has been subject to previous takeover interest with a merger proposal, and an agreement is reached, the target's management team is likely to experience abnormally high turnover 4 years later. The strong relationship between previous takeover interest in a target and the subsequent turnover of its top managers following a merger or acquisition in this instance lends support to the market efficiencies perspective (Fama, 1980). Absent performance measures for these managers, however, we cannot say for certain that the market for corporate control can identify and remove ineffective managers. Nevertheless, these results are consistent with such a theoretical interpretation. The time frame within which this turnover occurs is not surprising in light of the discussion above and effects for merger type and acquirer's approach. Pitts (1976) and Walsh (1988) both reasoned that the buyers of an unrelated company cannot afford to lose the unique and perhaps idiosyncratic talents of their target's managers in the short term — even if this 'talent' may have been subject to previous takeover scrutiny. The effect of the acquirer's approach is interesting in light of its correlation with method of payment (r=0.59, p<0.001). It seems that a merger paid for in stock will see high turnover in the fourth year. Table 2 reveals that a tender offer paid for in cash will see turnover earlier in the second year. In a tender offer–cash deal there may be immediate pressure on the target's managers to depart. The target managers' egos may be bruised or threatened by being circumvented in the transaction. Moreover, if the logic derived from Hansen (1987) is correct, the acquiring company is likely to be displeased to discover the relative poor quality of the target's managers. In a merger-stock deal, however, there may be no immediate pressure on the target's managers to depart. After all, the acquirer has worked with what may be a high-quality top management team to engineer the deal. Later turnover may reflect post-acquisition performance as much as pre-acquisition processes.

Future research directions

Nearly 50 percent of a target company's top managers turn over within 3 years of a merger or acquisition and we do not know why. Neither Walsh's (1988) examination of the relatedness of the acquisition nor the present look at the negotiations can explain the sizeable early turnover. Only the modest correlation between the hostility of the negotiations and subsequent turnover gives us any insight into the first year turnover at all. Clearly, additional work would be welcomed in this area. Most importantly, the market for corporate control perspective is in need of testing.

The slim evidence in this research that relates to the corporate control perspective is equivocal. If a high premium paid is to be associated with an undervalued company, then the negative correlations with subsequent top management turnover question this perspective. On the other hand, if previous merger and acquisition interest can be viewed as a market recognition of ineffective management, then its positive relationship with turnover would support this perspective. Although we wait for empirical research that tests the relationship between pre-acquisition company performance and subsequent management turnover, we continually find ourselves listening to this unsubstantiated logic as a justification for corporate takeovers. Carl Icahn, for example, recently explained his motives behind his corporate raiding:

> One of the hidden 'assets' in many companies is top management: get rid of them and the value goes up. What's going on in companies these days is absurd. It's like a corporate welfare state. We're supporting managements who produce nothing. No, it's really worse than that. Not only are we paying these drones not to produce, but we're paying them to muck up the works ('Icahn on Icahn', 1988: 58)

This kind of logic plays a central role in a good deal of takeover activity. As such, we urgently need research to assess its veracity.

Research that examines pre-acquisition company performance, post-acquisition management turnover, and their relationship to subsequent company performance is needed. If this next research effort indicates that we cannot explain the early departure of top managers by their own efforts and abilities, then we must examine an alternative hypothesis. It may be that the 'hubris' (Roll, 1986) or 'arrogance' (Jemison and Sitkin, 1986) of the parent company's managers explains the turnover of managers in their newly acquired company. A parent company may force out their target's top management simply because they believe they are somehow more capable than the target's managers, and because they have the power to act on this belief.

While the present research addresses top management turnover following mergers and acquisitions, it has also focused attention on merger and acquisition processes. Following Jemison and Sitkin (1986), this research is an attempt to understand the heretofore unexamined merger and acquisition-process. The present research represents but one attempt to understand the effects of one merger and acquisition process (i.e. the negotiations) on one outcome of some importance (i.e. top management turnover). Future research should investigate other aspects of the merger and acquisition process and other criteria of acquisition performance. Indeed, experienced consultants stress the importance of a well-managed pre-acquisition process to successful acquisitions (Fray *et al.*, 1984). As a beginning, Jemison and Sitkin (1986) developed 35 testable propositions concerning the impact of activity segmentation, escalating momentum, expectational ambiguity, and management system misapplication on acquisition integration. A logical research step would be to explore these ideas on the effects of the pre-acquisition process on later acquisition success.

A complete understanding of merger and acquisition processes also should include an understanding of the post-acquisition processes (Shrallow, 1985; Shrivastava, 1986). As noted, case study analyses tells us that the period immediately following an acquisition agreement can be a time of great organizational upheaval. We know very little about the effects of such upheaval on the individuals within these organizations, and on the organizations themselves. Indeed, Jensen (1984) searched, but could find little evidence for the impact of takeovers on plant closings, layoffs, and dismissals. Nevertheless, state legislators are being urged to enact laws to protect their local industries (and by extension, their communities) from takeover attempts (Miller, 1987). Research aimed at understanding the effects of mergers and acquisitions on middle managers, employees, and indeed, communities is needed.

CONCLUSION

The intent of this research has been to bring something of a process perspective to our understanding of mergers and acquisitions. Specifically, the effects of the pre-acquisition negotiations on subsequent target company top management turnover were investigated. With an acknowledgement that this examination of mergers and acquisitions is limited to target companies with assets in excess of $10 million, the descriptive evidence indicates that top management turnover is widespread. In addition to documenting the extent of the turnover, this research provided an interesting portrait of merger and acquisition negotiations.

From a theoretical perspective these results reveal some correlational support for many of the proposed relationships between the assessed properties of the merger and acquisition negotiations and subsequent target company top management turnover. The ANCOVA analyses, however, indicate that the full impact of the negotiation process is felt 4 years after the settlement date. Just the same, much of the value of this research lies in what the results do not say, as opposed to what they do say. Taken together, these results indicate that the merger and acquisition negotiations fall short of explaining a good deal of subsequent target company top management turnover. This is especially true of the important, early post-merger turnover. The clear task for future researchers is to understand the origins of this sizeable early turnover following a merger or acquisition. The study of both the market for corporate control perspective and the post-merger integration period offers the most research promise.

It has been estimated that more than one-half of all mergers and acquisitions fail (O'Connell, 1985). We can only hope to understand the origins of these failures (and successes) with a continued evolution in our understanding of strategic and organizational fit and, indeed, the merger and acquisition process itself.

ACKNOWLEDGEMENTS

The author would like to thank Sue Ashford, Vijay Govindarajan, Dave Jemison, Dave Schweiger and Debra Shapiro for their helpful comments on an earlier version of this paper, and Kathy Jardine for her help in collecting these data. The financial support of the Tuck Associates Program is gratefully acknowledged.

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