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Cultural Factors in International Mergers and Acquisitions

When and Where Culture Matters

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Abstract: Existing studies on IM&As take mostly a finance or economic perspective, measuring the outcomes of IM&As in the short term while ignoring their long-term returns and non-financial factors. The present research is designed in response to this shortcoming, examining the effects of culture on the outcome of IM&As and the variation of these effects during the different phases of an IM&A. The research focuses on the international aspect of cultural differences—the differentiating factor between domestic mergers and acquisitions (M&As) and IM&As. It measures success from an organization's internal perspective, comparing what the IM&A, at inception, was expected to achieve and what it achieved several years later. This approach is different from the standard one of measuring success based on market reaction to the IM&A—an external measure. This qualitative research is based on an interpretive approach, cutting across economic, international business, and behavioral theories. The significance of the study lies in its emphasis on national culture as a construct separate from organizational culture, in measuring the success or failure of an IM&A relative to its objectives, and in supporting reflexivity theory in economics.

Keywords: International Mergers and Acquisitions, Cross-Cultural Management, Cultural Differences

Introduction

OVER THE PAST two decades, cross-border or international mergers and acquisitions (IM&As) have become the preferred method of foreign direct investment (FDI). The trend shows that IM&As go both ways: *toward* developing countries and *from* them, reshaping the world's economic boundaries (Chapman, 2003). Trends notwithstanding, researchers suggest that, overall, the expected financial benefits of M&As are often not realized (Auster & Sirower, 2002).

The high rate of failures has been associated mainly to the fact that "M&As are still designed with business and financial fit as primary conditions, leaving psychological and cultural issues as secondary concerns" (Bijlsma-Frankema, 2001, p. 192). While as new countries enter the free-market economy, paying attention to cultural factors in IM&As is becoming crucial (Rondinelli & Black, 2000). The wider cultural gap and the current trend of IM&As between developed and developing countries increases the urgency of understanding the effects of culture on the dynamics of IM&As and on issues such as corporate governance and local adaptation strategy.

The present research is designed in response to this shortcoming. It examines the effects of culture on the outcome of IM&As and the variation of these effects during the different phases of an IM&A. The research focuses on the international aspect of cultural differences—the differentiating factor between domestic mergers and acquisitions (M&As) and IM&As. It measures success from an organization's internal perspective, comparing what the IM&A, at inception, was expected to achieve and what it achieved several years later. This approach is different from the standard one of measuring success based on market reaction to the IM&A—an external measure.

Related Theories

The main argument of this research is that there is no single way of managing across borders. People's perceptions and interpretations of their environment and, therefore, their rationality, are affected by cultural factors. Different perceptions and interpretations result in different decisions and behaviors. Cultural differences affect our view of business and management and, consequently, the outcome of IM&As. When complementary to the objectives of an IM&A, cultural differences may be an asset. When in conflict, they will be a liability and a risk factor. Either way, national cultural differences should be accounted for and planned for so as to reduce the risk of failure and increase the chances of success. This argument is based on the reflexivity theory in economics, as proposed by Soros (1987), which assumes that people have biases and that they make decisions based on incomplete information. This is in contrast to the equilibrium theory in economics, which assumes that information is immediately distributed to everyone, that people seek to maximize profit, and that they behave rationally. Implicitly, the equilibrium theory assumes that rationality is similar across cultures (Umpleby 2006). Cultural differences, which can be regarded as a form of bias, fit easily within reflexivity theory but tend to be neglected within a perspective guided by equilibrium theory.

Literature Review

Despite two decades of increasing M&A activity, both within and across countries, researchers have neglected cultural factors or have treated organizational culture and national culture as *one* factor. Moreover, none of the studies have focused on the role of national culture in an IM&A process.

Double Layer—National and Organizational—Culture

Cultural factors in IM&As can be studied at both the organizational and the national levels. These two levels of culture should be treated as separate variables to show how they relate to other aspects of IM&As (e.g., organizational structure, performance, and acculturation). Larsson and Lubatkin's (2001) assessment shows that most researchers (1) have treated organizational and national culture as one factor in their analyses; and (2) have concluded that culture clash results in a decline in shareholder value at the buying firm, it affects organizational restructuring, it causes a deterioration of operating performance at the acquired firm, it lowers employee commitment and cooperation, and it results in greater turnover among acquired managers.

Acknowledging the importance of culture in the success of IM&As, researchers have recommended a harmonious integration of the beliefs and values of merging firms and say that the ability to integrate organizational cultures (i.e., achieve acculturation) is more important to merger success than financial or strategic factors. In summary researchers consider cultural synergy an important success factor (e.g., Marks and Mirvis 2001). However, most researchers have treated culture at the organizational level and discussed success factors of cultural integration in M&As with the exception of few (e.g., Rondinelli and Black 2000) who have treated culture at the national level but have analyzed IM&As and trends in a specific region.

A few researchers who acknowledge that national and organizational cultures act at different levels still include them in their analysis as one factor. One of the most cited studies is Malekzadeh and Nahavandi's (1998) work on the role of leadership in IM&As. They acknowledge that acculturation takes place at two levels, national and organizational—a concept that has been called a double-layered acculturation process. However, they consider both levels of culture as part of the leader's mindset, with a major impact on the acculturation course leading to the eventual success or failure of the merger.

In summary, researchers seeking to understand the process and outcome of the IM&A with culture as an important factor (among others) are divided in considering national culture as a separate factor or as part of the organizational culture. While cultural fit has been acknowledged to be a potentially important factor in M&As, the concept is ill defined, with no distinction drawn between the national and corporate levels of culture.

Distinguishing Organizational Culture from National Culture

One way to draw a line between the two levels of national and organizational cultures is by using Schein's (1985) cultural model. Corporate culture can modify the first two levels in Schein's model—(a) behavior and artifacts and (b) beliefs and values—but it is not capable of affecting the third, deeper level of the core assumptions that are derived from one's national culture (Weber et al., 1996, p. 1216).

Another way to separate national culture from the organizational one is to use Hofstede's work. His six dimensions of organizational culture and his four dimensions of national culture show the differences between the two layers of culture (Hofstede, 1997, p. 188). His national cultural dimensions include power distance, uncertainty avoidance, individualism/collectivism, and masculinity/femininity. His organizational cultural dimensions are process-oriented/result-oriented, employee-oriented/job-oriented, parochial/professional, open/closed system, loose/tight control, and normative/pragmatic. These two groupings of cultural dimensions reflect different layers of culture. In the data generated for this study, these definitions have been used to separate national culture from organizational culture and then focus on national culture where the gap in literature resides.

Importance of National Culture

National culture sets the direction of how foreign investors are perceived by the host country and defines the host government's preferences in economic and social forms and consequently in its trade policies. Through their institutions, nations affect the norms according to which buying firms manage the post-acquisition process. The influence of national culture on acculturation of IM&As might be hard to specify empirically, but also hard to deny (Larsson and Lubatkin, 2001). To support this argument, Larsson and Lubatkin compare Swedish and American cultural preferences in IM&A. They argue that Swedish buying firms are more likely than American buying firms to achieve acculturation.[1] Swedish firms, they say, are more likely than U.S. firms to govern the postacquisition process in ways that minimize culture clashes and improve the likelihood of achieving acculturation (e.g., egalitarianism, collective responsibility, cooperation, jointly negotiated agreements, and voluntary compliance).

Another example of the importance of national culture is offered by Koveos (1997) who compares the American attitude with that of the Japanese in their respective objective functions. Many in Japan would say that companies exist to benefit their employees. Firm activities, then, must take the welfare of employees into consideration. As a result, methods viewed as typically American, such as hostile acquisitions through tender offers or proxy battles, are generally not found in Japan. These examples indicate the difference in management approach. They show "two conflicting forces: on one side, the financial aspect, effectiveness and efficiency, and the importance of shareholders; on the other side, the social aspect, human resources, and personnel" (Koveos, p. 72). An IM&A has to address all these aspects and find balance in managing these differences, a task that requires ongoing adjustments as the degree of importance of these factors changes during the stages of the IM&A process and varies from one industry to another.

The present study selects the first step of an IM&A—the choice of investment location and mode of market entry—to illustrate an example of the effects of national culture on IM&As. In this first step, home-country national culture influences a firm's choice of foreign-entry mode (e.g., M&A, joint venture, or alliance). Executives of different nationalities have a different perception of risk, which affects their evaluation of a merger. The perception of risk or their attitude toward uncertainty is one of the national cultural dimensions that allows one to measure cultural differences. Empirical research shows that uncertainty avoidance affects the investor's choice of entry mode into a foreign market (e.g., Kogut and Singh, 1988).

Research Perspective

M&A research falls under the four categories of (a) event studies (or market-based return to shareholders), (b) accounting studies (returns estimated from financial statements), (c) survey studies, and (d) clinical or case studies (Bruner, 2004). M&As stir interest in different disciplines (i.e., accounting and finance, organizational behavior, international business, strategy, and management). A review of the existing empirical studies of M&As shows that although many areas have been extensively researched, others—such as the long-term effects of mergers—remain practically untouched (Andrad et al., 2001). The range of research on M&As extends from motivations for an M&A to the reasons for failure or success. Some researchers have focused on the motivations for M&As from the synergy, agency, and hubris perspectives.[2] Others have studied motivation from the perspective of reducing uncertainty.[3] The argument is that, overall, a merger is a way of internalizing the needed resources or the combined competencies under one organization. *Control* is the main factor differentiating M&As from joint ventures or licensing. Internalization enables a firm to control its resources and its market and to reduce its dependency. (For a definition of terms, including the difference between M&A and IM&A, see appendix, Table 3.)

Most researchers (whose primary field is often finance or accounting) have analyzed mergers from a *static* point of view, a snapshot of market reaction—called *event study*—after the merger is announced (Brown & Warner, 1985). They ignore the *dynamic* process of conducting a merger. Research conducted from the dynamic, management perspective of M&As will shed light on a merger's multilayered and interactive environment. It will provide a better understanding of what contributes to a merger's success or failure and where and how in the process of a merger these contributions take place. This research is designed from this dynamic perspective to fill the gap in literature and contribute to the existing knowledge of IM&As.

Research Questions, Assumptions, and Proposition

Research Questions

Primary research question:

- Do national cultural differences affect IM&As' success or failure?

Secondary research questions:

- Where, in the process of an IM&A, are the effects of national cultural differences most significant?

[1] Everything else held constant, assuming that Swedish firms represent a microcosm of Swedish society, thus reflecting its beliefs.
[2] Respectively: economic gain from two firms' resources, satisfying the acquiring management's welfare, and managers' lack of judgment for embarking on a merger without a business or economic rationale.
[3] The uncertainty reduction theory holds that compared with other ways for two firms to share their specific advantages (e.g., joint venture or licensing), a merger offers higher uncertainty reduction (Lubatkin & O'Neil, 1987).

- What methods could be used for managing the effects of national cultural differences on an IM&A's outcome?

Proposition

The greater the cultural differences between the country of the investing firm and the country of the acquired firm, the higher the chances of failure (or the lower the chances of success) of an IM&A.

Research Approach

The approaches used are ethnographic and interpretive. The ethnographic approach's epistemological assumption is that culture can become known through social settings, while the interpretive approach uses people and their interpretations, perceptions, meanings, and understanding as the primary source of data. The interpretive approach supports a study that uses interview methods, for example, where the aim is to "explore people's individual and collective understandings, reasoning processes, social norms, and so on," (Mason, 2002, p. 55). Based on this interpretive approach, in-depth discussions have been conducted to collect information and generate data. Information has been collected from individuals at the decision-making level of organizations that have completed IM&As and from individuals mediating IM&As.

Research Method

In existing IM&A studies, success or failure is measured based on financial results and short-term market reaction. This method, independent from the IM&A's objectives, does not offer any measure of the long-term success of IM&As. To fill this gap, the present study used a method of measuring an IM&A's success both from an internal perspective and in relation to its original objectives. The argument is that market reaction is based on financial speculation while the IM&A's objectives could be other than financial gain (e.g., strategic positioning, oligopoly); therefore, measuring the IM&A's performance against its original objectives could provide meaningful and practical findings.

The research method has been selected based on the following factors:

- Lack of existing data on cultural factors in IM&As
- Use of this method by other researchers and, consequently, its approval (Auster & Sirower, 2002; Bijlsma-Frankema, 2001; Erez-Rein, Erez, & Maital, 2004; Kogut & Singh, 1988; Koveos, 1997; Larsson & Lubatkin, 2001; Nahavandi & Malekzadeh, 1988; Rondinelli & Black, 2000; Weber et al., 1996)
- Fit of the method to research studying the practical aspects of IM&As. A qualitative research method is a better fit for studies of "things that matter, in the ways that matter" (Mason, 2002, p. 1)

The proposed method relies on managers' perception and evaluation of their success. The result of this research shows that managers are candid in providing information and willing to participate. The present research method can therefore be replicated for an empirical analysis based on a wider sample.

Data Generation

Data was generated through informal—but topic-oriented and qualitative—in-depth discussions with individuals. Research questions and the survey instrument were tested on two pilot companies to select the best way of capturing trustworthy insights. The test included three different methods for collecting data:

- Having managers complete the questionnaire
- Asking the questions in sequence and having the interviewer fill out the questionnaire
- Carrying out a guided conversation, making sure that all the questions were answered, but allowing the interviewees to talk as they chose

In both pilot companies, the open discussion proved to be more effective than asking the interviewees to answer questions in a predefined order. The selected method comprised leading the discussion to ensure that all questions were answered, but allowing the interviewees to talk and explain their experiences in their own ways and according to their cultural preferences.

The term *data generation* is used instead of *data collection* because of the research perspective and the interpretive approach. Most qualitative perspectives reject the idea that a researcher can be a completely neutral collector of information about the social world (Mason, 2002). To overcome this weakness, the researcher stayed unbiased regarding the outcome of the present research and remained neutral and as objective as possible in interpreting interviewees' comments. To ensure neutrality, a colleague was asked to review and validate interpretations.

Research Validity

Generalizability and trustworthiness of empirical research depend on its reliability, internal validity, and the external validity of measures and procedures.

The corresponding terms in naturalistic inquiry are auditability, credibility, and fittingness[4].

To make this research auditable—or transparent, as some researchers call it—a clear data collection and data generation process were developed and followed. To ensure consistency of the process, a detailed research journal, interview notes, and analysis of each interview session were systematically kept.

To increase the credibility of this work, a well-defined interview procedure was developed. Two interviews were conducted with each individual and additional ones scheduled when needed. In addition, throughout the research, the interviewer was available and in contact with interviewees by telephone and e-mail to make sure that their experience and reflections were captured accurately. Voice records of interview sessions, transcripts, interview notes, and session analyses were systematically compared and a summary of the interview sent to the interviewee for validation. These steps ensure the credibility of the research, or consistency-coherence, as some researchers call it.

To comply with fittingness requirement, the research sample was selected from trustworthy reports, based on criteria explained in the data sample section. As for the thick description and communicability of the research, findings will give the reader an explanation of the effects of cultural differences in the process of an IM&A. This process is common in all IM&As. These findings are therefore, to some extent, generalizable to other IM&As.

Research Measures

Measuring Cultural Distances

The index used to measure cultural distance is a composite index based on cultural dimensions to measure national cultural distances. This method has been used by others such as Kogut and Singh (1988). Studying American firms' IM&As, Kogut and Singh used a composite index of cultural dimensions to measure the cultural distance between the investing firms. Using cultural dimensions indexes, they formed a composite index based on the deviation along each of the four dimensions of each country from the U.S. ranking. They then corrected the deviations for differences in the variances of each dimension and calculated an arithmetic average (Kogut & Singh, p. 422).

The composite cultural distance index (CDI) is based on four cultural dimensions[5] that best reflect the differences between countries and most affect organizational culture (Hoecklin, 1996). The CDI is based on the deviation of each of the four cultural dimensions of each country from the ranking of the country of the sample or the country of investigation. For example, assuming that the sample includes IM&As of firms from country *X* with those from countries *A*, *B*, and *C*, the deviations of each of the four cultural dimensions of countries *A*, *B*, and *C* from the ranking of the corresponding dimensions of country *X* were calculated. The deviations were then corrected for differences in their variances. Equation 1 illustrates the calculation of power distance (*PD*) deviations between countries *A* and *X*:

$$PDI_A = (PD_A - PD_X)^2 \,/\, PDV \qquad (1)$$

in which *PDI a* stands for the power distance index for country *A* in relation to country *X*, and *PDV* is the variance of power distance in Hofstede's indexes. Similar equations were used to calculate the deviation of the other three cultural dimensions of country *A* from related dimensions of country *X*.

Then, the cultural distance (*CD*) for country *A* in relation to country *X* was calculated, using Equation 2:

$$CD_A = \sum_{i=1}^{4} \{(I_{iA} - I_{iX})^2 / V_i\} / 4 \qquad (2)$$

[4] (1) The corresponding term of reliability in empirical research, auditability refers to consistency of procedures in a way that another person could understand the themes and arrive at similar conclusions; (2) Credibility in naturalistic research is the corresponding term for internal validity in empirical research: validity of a causal inference. Credibility is achieved through structural validation by spending sufficient time with interviewees to check for distortions and explore their experience in sufficient detail; (3) Fittingness, or communicability, refers to the generalizability of the findings. It is the corresponding term of external validity in empirical research. A qualitative study emphasizes the thick description of a relatively small number of participants within the context of a specific setting. The amount of data collected is considered adequate when the researcher reaches saturation. Additional conditions for fittingness are appropriateness, audit trial, and member check. Appropriateness of the research refers to purposeful—versus random—selection of the sample (Rudestam & Newton, 2001, p. 98).

[5] Power distance (PD), uncertainty avoidance (UA), collectivism/individualism (CI), and universalism/particularism (UP) or L-term/Short-term orientation (LTO/STO)

in which *CD a* stands for the cultural distance of country *A* from country *X*, and *Ii a* is the index for the *i*th cultural dimension of country *A*. This calculation was then replicated for countries *B* and *C* (countries in the sample for which CDIs exist).

Measuring Success/Failure

The overall objective of the research is a better understanding the contribution of national cultural factors to the success or failure of the undertaking. The method used is similar to Cantril's (1965) Self-Anchoring Striving Scale[6] to measure the overall performance of an IM&A and the contribution of cultural factors to performance. Relying on their judgments—while validating them with hard data, when possible—managers were asked the following questions:

- What were their best and worst expectations of the possible outcomes of an IM&A? They were asked to rate these scenarios on a spectrum of 10 to 0.
- Where, on the above spectrum, did they think this IM&A would come out?
- Where do they think it stands now?
- Where do they think it will be in five years?

The managers were then asked to estimate the contribution of cultural factors to the above scores; in other words, estimate how much of the shifts of the present and future scores from the original estimate were due to cultural factors.

The above questions covered the research interest of measuring success or failure from an IM&A's *internal* perspective and in relation to IM&As original objectives and expected outcomes. In addition, interviewees were candid in sharing their evaluation of what had been achieved and what they thought would be achieved within the next five years and comparing it with the ideal outcome.

Research Sample and Data

Research Sample

The focus of the research was Brazil because it is one of the developing economies attracting foreign direct investment (FDI). Among host developing economies, three quarters (75 percent) of the top transnational corporations (TNCs) have affiliates in Brazil (UNCTAD [United Nations Conference on Trade and Development], 2005). The selected companies are IM&As from countries at the two ends of Brazil's cultural distance index (CDI) spectrum.

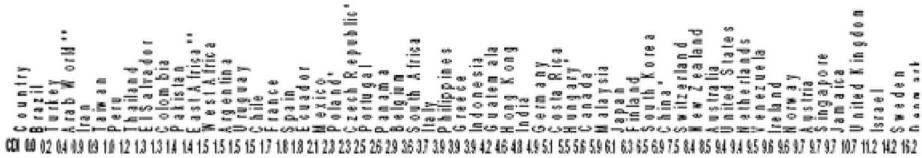

Figure 1: Brazil Cultural Distance Index (CDI) Spectrum

Individuals and groups within each organization[7] have been selected from managers at the decision-making level who are aware of the organization's strategy and are able to explain both the positive and the negative effects of cultural differences during different phases of the IM&A. Twelve managers participated in the research: six from the culturally high-distance countries and the other six from low-distance countries. To gain additional insight into the cultural issues of an IM&A and to support the findings from the IM&As group, 11 individuals who have formerly been involved in IM&As were also interviewed. These additional people include retired executives who have been through several IM&As, as well as consultants and professionals who mediate IM&As and are considered experts in helping foreign investors in Brazil.

The data was collected from each individual in two sessions. When needed, additional sessions were scheduled. When possible, each interviewee was asked to answer each question from three different perspectives: (a) as it relates to him or her; (b) as it applies, in general, to the interviewee's colleagues from his or her own legacy company and nationality; and (c) as it applies, in general, to his or her colleagues from the foreign counterpart company and nationality. The purpose of asking the questions from these perspectives was to see to what extent each issue had been discussed and shared with others. At the beginning of the interview, the ranking system

[6] Cantril's (1965) Self-Anchoring Striving Scale method of capturing the state of mind of individuals is based on several questions. A person is asked to define, on the basis of his or her own assumptions, perceptions, goals, and values, the two extremes or anchoring points of the spectrum on which some scale of measurement is desired (e.g., the top and bottom, the good and bad, the best and worst). This self-defined continuum is then used as the measuring device. For example, Cantril says, "one can determine a person's expectation of life by asking five questions: (a) what is the best possible life you can imagine for yourself in the future? Give that a score of 10. (b) What is the worst possible life you can imagine? Give that a score of 0. Within this spectrum, (c) where would you say you stand at the present time? (d) Where did you stand five years ago? and (e) Where do you think you will be five years from now?" (Cantril, p. 22)

[7] 60 companies meeting the research criteria were contacted

in answering each question was also explained: strongly agree / extremely important; agree / very important; agree to some extent / moderately important; disagree / a little important; strongly disagree / not important

The questionnaire includes 27 questions in five categories:

1. Corporate governance as it relates to cultural differences, to understand to what extent governance and control are culturally accepted by both sides of IM&A
2. Measuring the IM&A's success or failure
3. The effects of cultural factors on its success or failure
4. The variation of cultural effects in phases of IM&A
5. Overall recommendations

The research data were generated from 3,420 minutes (57 hours) of discussion sessions. Table 1 includes a summary of research data:

Table 1: Research Sample

Unit	Number	Description
Country	1	Brazil, a country with three quarters (75%) affiliates of the top transnational corporations (TNCs) (UNCTAD, 2005)
Organization	11	From the selected country: 5 from the most culturally different IM&As; 6 from the least culturally different IM&As
Individuals	12 IM&A managers	The main sample includes equal numbers of individuals from the high- and low-CDI groups: 6 from high CDI; 6 from low CDI
	11 others	These individuals were added to the sample for additional insights. They are retired executives and experts in IM&As. In this analysis, they are treated separately because they have an unequal distribution (high and low CDI): 8 high CDI; 3 low CDI
Discussion sessions	Individual: 23	Introduction to the research running 60 minutes (on average) Main discussion (interview) sessions running between 45 and 130 minutes
	Introduction: 1,380 minutes / 23 hours	
	Interview discussion: 2,040 minutes / 34.0 hours	
	Total: 3,420 minutes / 57 hours	

Research Data: High- and Low-CDI IM&As

The research sample includes an equal number of IM&A interviews from high and low CDI. The difference, if any, between cultural effects in the success or failure of these two groups will confirm or reject the proposition of this research. To test the research proposition, a compiled case for the high-CDI IM&As and another one for the low-CDI IM&As were created, as shown in Table 2 (two cases of IM&As). The following section discusses research findings for these two cases—labeled "case A" and "case B."

Table 2: Two Cases of IM&As

Two Cases of IM&As				
Interview		CDI		IM&A Profile
#	Country of Origin / Counterpart	Number	High / Low	
Case A: High-CDI IM&A				
3	Brazil / U.S.	9.4	H	Automotive and technology industry; manager also involved in several previous mergers of U.S. companies in Brazil
9	Brazil / U.S.	9.4	H	IT industry
11	U.S. / Brazil	9.4	H	IT industry
19	Brazil / U.S. (a)	9.4	H	Plastic transformation industry (manufacturer of packages for different segments)
20	U.S. / Brazil (a)	9.4	H	Plastic transformation industry (manufacturer of packages for different segments)
21	Brazil / Sweden	14.2	H	Pulp and paper, chemicals, and specialty products
Case B: Low-CDI IM&A				
1	Brazil / Chile	1.5	L	Chemical industry (interviewee from Australia)
4	Brazil / Argentina	1.5	L	Consulting in FDI, training; subsidiary of a merged company, helping more than 100 companies merging and acquiring Brazilian companies
6	Argentina / Brazil	1.5	L	Foreign trade, logistics, customs, and transportation services
7	Argentina / Brazil	1.5	L	Oil industry
10	Brazil / Spain	1.8	L	Market research, formed from a group of companies from around the world
15	Lebanon / Brazil	0.4	L	Consulting, specializing in international assignment infrastructure

Findings

The differences and similarities of these two cases are summarized under six topics of cultural factors and corporate governance, double identity and cultural adaptation, national and organizational cultures, cultural factors and IM&As' success, cultural factors in phases of IM&As, and overall effects of cultural factors.

Cultural Factors and Corporate Governance

Interview questions related to this topic show the differences between cases A and B (appendix, Table 4). Based on the differences between high and low CDI statistical results and managers' comments, we can conclude that:

- In low-cultural-distance IM&As, managers are more comfortable than in high-cultural-distance IM&As to see more control transferred to the subsidiary (territory).
- Low CDIs have a stronger preference in reducing regulation gaps between home and host countries.

Double Identity and Cultural Adaptation

Findings of related questions show the difference between cases A and B on how managers see and adapt to the two levels of national and organizational cultures (appendix, Table 5). Based on the differences between high and low CDI statistical results and on managers' comments, we can say the following:

- Managers of IM&As with high CDIs have a stronger preference for subsidiary adaptation to headquarters than managers of IM&As with low CDIs.
- The higher the national cultural distance, the more visible and recognizable a double identity.

National and Organizational Cultures

Based on the differences between high and low CDI statistical results and on managers' comments (appendix, Table 6), we can conclude that:

- Organizational culture reflects national culture. There are common cultural characteristics among

firms of a country, despite differences in their organizational cultures.
- Higher cultural distance has a slightly higher effect on investment decisions of managers from low CDI countries.

Cultural Factors in IM&As' Success

One of the questions related to this topic shows the difference between high and low CDI responses (appendix, Table 7). In conclusion, managers of high-CDI IM&As strongly agree that objectives of an IM&A should be clearly defined and shared. While it is understood that strategic objectives can be kept at a top executive level, there is agreement that operational objectives must be shared before the implementation of the merger. This conclusion is also reflected in managers' comments.

Cultural Factors in Phases of IM&As

Finding of related questions show a difference between IM&As from high and low CDI countries (appendix, Table 8).

Based on statistical results and managers' comments, we can conclude the following:

- The higher the cultural distance, the stronger the agreement that cultural factors should be accounted for in the due diligence process.
- For both high- and low-CDI IM&As, the importance of cultural differences is greatest in phase 1, less in phase 2, and least, but equal, for the remaining phases.
- It is important for both high- and low-CDI IM&As to include cultural factors in designing IM&As' structure.
- It is equally important for both high- and low-CDI IM&As to have a strategy and a plan to manage cultural differences.

Overall Effects of Cultural Factors in IM&As

Findings of interview questions related to this topic show the difference between high- and low-CDI IM&As (appendix, Table 9).

Based on the results and managers' comments, we can conclude the following:

- The lower the cultural distance, the higher the perception of cultural factors' risks.
- Lower cultural distance is an additional advantage (an asset), while higher cultural distance is a disadvantage (or liability).

Summary Differences

The differences between IM&As from high and low CDIs (or between cases A and B) can be summarized as follows:

- In high cultural-distance IM&As, managers
  - are less comfortable than in low cultural-distance IM&As to see more control transferred to the subsidiary (territory).
  - have a stronger preference for subsidiary adaptation to headquarters than do managers of IM&As with low CDIs.
  - have a slightly higher perception of cultural risk affecting their investment decisions than do managers from low-CDI countries.
  - have stronger agreement that operational objectives of an IM&A should be clearly defined and shared before implementation of merger.
  - have stronger agreement than do managers of low-CDI IM&As that cultural factors should be accounted for in the due diligence process.
  - have a lower perception of cultural factors' risks than do managers of low-CDI IM&As.
- It is equally important for both high- and low-CDI IM&As to have a strategy and a plan to manage cultural differences, as well as to include cultural factors in designing IM&As' structure.
- For both high- and low-CDI IM&As, the importance of cultural differences is greatest in phase 1, less in phase 2, and least, but equal, for each of the remaining phases.
- The higher the national cultural distance, the more visible and recognizable a double identity.
- Lower cultural distance is an additional advantage (an asset), while higher cultural distance is a disadvantage (or liability).

Discussion on Research Questions

National Cultural Differences in IM&As' Success or Failure

The research sample included two groups of high and low culturally distant IM&As in a single host country (cases A and B, Table 2). The contrast between responses from these two groups and the ensuing findings confirm that national cultural differences affect IM&As' success or failure. This confirmation is based on the following findings and examples:

- The higher the cultural distance (CDI):
  - The stronger the opinion that the IM&A's strategic objectives should be kept at the high managerial level, but that operational object-

    ives must be shared before implementation with managers on both sides
  - The more visible and recognizable the layers of identity
  - The higher the transaction and coordination costs
- The lower the cultural distance (CDI):
  - The higher the compatibility of cultural factors
  - The more comfortable managers are in transferring more control to the subsidiary

Variation of Cultural Effects on the Phases of IM&A

The importance of cultural differences decreases in the different phases of a merger, being greatest in phase 1, less in phase 2, and least, but equal, for each of the remaining phases. Managers should pay close attention to cultural factors at phase 1 (before IM&A and at the planning stage) and at phase 2 (implementation).

Methods for Managing the Effects of National Cultural Differences

Managers mentioned IM&As' structure as one method of coping with national cultural differences. These methods are mainly the IM&As' managerial approach and hierarchy in reporting and control. Selecting a home country (ethnocentric), host country (polycentric), regional (regiocentric), or world (geocentric) approach helps to cope with cultural differences.

Conclusion

The differences between the findings in cases A and B confirm that national culture is a separate construct from organizational culture and affects IM&As at a different level. So far, its effects and costs have been generally ignored, but, as this research shows, it is imperative to measure and include national culture in the investment business plan. These research findings show that IM&A's return on investment might have been higher if culture is incorporated into business plan; therefore, whether an IM&A creates value or not should not be the whole issue. Cultural differences have an impact on IM&As success. Practitioners can use the results of the study in their due diligence evaluations and IM&A implementations. Also, international and overseas investment guarantee organizations (e.g., the World Bank's Multilateral Investment Guarantee Agency [MIGA]) involved in promoting FDI in developing countries can use the results of this research to evaluate a business plan for foreign investment and an investor's management plan for cultural issues.

Practical Implications

The purpose of this research was to show the need to include cultural differences in an IM&A's business plan, along with financial and economic factors. Managers should give the same consideration to cultural differences that they give to other aspects of the business (e.g., financial factors).

IM&A's Success

The chances of an IM&A's success can be greatly enhanced when the following steps are taken:

- Include cultural factors in the business plan, along with financial and economic factors.
- Understand the two layers of culture (national and organizational); develop a strategy and a plan to manage organizational culture and to accept and account for the cost of what cannot be changed (national culture).
- Preserve the IM&A's standard global image, brand, and reputation, but learn how to communicate them to the local market.
- Keep the strategic objectives of the IM&A at a high executive level, but share the operational objectives before implementation with all levels of managers from both sides of the IM&A.
- Develop realistic objectives and strategic, structural, and implementation plans based on cultural differences.
- Communicate the IM&A's value to both sides.
- Include cultural factors in the due diligence evaluation and measure their effects in terms of cost and based on their impact on the bottom line.
- Select the right person to lead the operation: someone who understands both the strategic objectives of the IM&A and the host country culture.

Manager Success

From an international management perspective, chances of success are greater when managers do the following:

- Understand cultural differences, have empathy in a nonjudgmental way, and construct a reasoning based on both cultures.
- Identify how the home country is perceived by the host country. Develop a strategy to overcome any negative existing image and benefit from the positive one. One example provided by a manager is that she realized that her compatriots are perceived in the host country as being ethical and respectful of their contracts. She used this perception as a competitive advantage and positioned her company as the most ethical one, delivering its promises to the host country (within its industry). At the beginning, she said, it was diffi-

cult to be ethical because bribery and changing and modifying contracts were—and still are—the norm. There was a cost associated with being ethical, but she saw it as an investment that paid off in the long term.

Research Limitations

- The findings of this study and the method of investigation can be used as a framework for future empirical study of IM&As. Future research could be designed to overcome the following limitations by increasing the sample size:
- Controlling for size of IM&As: The research sample includes IM&As from small and medium organizations. A larger sample would allow investigating and controlling for the effect of the size of the company.
- Controlling for industry: Another limitation is the mix of industries. The effect of cultural differences will vary depending on the industry and on the level of the IM&A's interaction with the host country.
- Accounting for business and economic cycles: IM&As operate within the economic cycle of home and host countries, which affects performance. They also follow a business cycle that needs to be accounted or controlled for in any comparative study.
- Leveraging on bargaining power: As one of the interviewees mentioned, IM&As' competitive advantage matters in determining the level of adaptation to host country culture. Adaptation to host country or internalization of cultural differences is costly. A foreign investor has a higher bargaining power when its products or services are needed in the host country. This competitive advantage allows the investor to avoid adaptation costs. A larger sample would allow the researcher to control for the investor's bargaining power and would offer insights on how investors use their competitive advantage to impose their culture and avoid cultural adaptation and integration.
- Overcoming language barriers: Language was not an issue in this research because all interviewees were bilingual (English and Portuguese). In addition, a bilingual translator was present in all interviews. However, a larger sample would involve interviewing managers in different countries, possibly in different languages. Any future research needs to pay close attention to the language barrier in a multilingual environment.

Significance of the Research

The significance of the study is both *theoretical* and *practical*. The first theoretical significance lies in providing support for reflexivity theory vis-à-vis equilibrium theory in economics. Second, the study advances the proposition that national culture matters in the success or failure of an IM&A. Third, the study distinguishes national culture from organizational culture in the M&A process (these two cultural factors have traditionally been taken as one in IM&A research). Fourth, the study explores the variation of cultural effects during the IM&A process. By relating cultural factors to the process of managing an M&A, this study provides an explanation of how and where culture matters.

The practical significance of the study is its potential for exploring ways of managing cultural differences and shedding light on some cultural issues of IM&As, as expressed by executives involved in IM&As. For example, "executives have associated the failure of their IM&A operations to the widely varying expectations of managers and their different management styles" (Gancel, Rodgers, & Raynaud, 2002, pp. 211–221). Such circumstances are "caused by both corporate and national culture gaps, leading to misunderstanding and conflict and, ultimately, to the failure of the IM&A" (Kühlmann & Dowling, 2005). An awareness of these factors may help mitigate some of the risks inherent in the undertaking.

Future Research

This qualitative research method and its findings show that it is possible to measure an IM&A's success and failure from an internal perspective. The managers who were interviewed were candid at sharing their evaluation of their IM&A's outcomes and at providing meaningful insights. The research can be replicated with a larger sample, in future empirical studies covering multiple countries and industries. The sample should include several managers within each IM&A and from both sides of the merger. This will allow the researcher to see the differences in how the two sides of the merger experienced the integration, how each side overcame the cognitive imbalance created by the integration process, and how they regained or created a new stage of cognitive balance.

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Appendix

Table 3: Definitions of Terms

Definitions of terms	
Culture	Defined as the collective programming of mind and mental framework (Hofstede, 1984); referring to shared attitudes, beliefs, and values defining and directing human behavior in social systems (Triandis, 1998; Walter, 1985), based on common philosophies, ideologies, perceptions, and expectations (Kilmann, Saxton, & Serpa, 1985) shared among most organizations belonging to the same culture or country.
Cultural difference	As measured by the cultural dimensions of Hofstede (1994, 1997): power distance, uncertainty avoidance, masculinity/femininity, and individualism/collectivism; by Trompenaars & Hampden-Turner (1998): attitude toward time and environment, and relationship with people; by Schwartz (1994) and by Schwartz & Smith (1997): conservatism, intellectual autonomy, affective autonomy, hierarchy, egalitarianism, harmony, and mastery; and by Triandis (1998): definition of the self, structure of goals, emphasis on norms versus attitudes, and emphasis on relatedness versus rationality.
Cultural distance	Measured by a composite index (Kogut & Singh, 1988) of four cultural dimensions best distinguishing nations and most affecting the organizational culture (Hoecklin, 1996, p. 47): • Power distance: the degree of acceptance of unequal distribution of power among people. • Uncertainty avoidance: the way people cope with the unexpected. • Collectivism/individualism: where do people's preference lie, with the individual or with the group? • Universalism/particularism: which prevails: rules or relationships? In particularism, unique situations and relationships are more important in determining what is right and good than rules.
Merger and acquisition	Refers to a legal transaction of either transferring all assets of one firm to another or joining together all the assets of two firms into a single new organization (Gertsen et al., 1998, p. 17). In M&A literature, the terms merger and acquisition are used interchangeably (Olie, 2005, p. 333). These two terms are used together, particularly when the research focuses on the sociocultural or nonfinancial aspects of bringing two organizations together. This study will use merger and acquisition as one concept because the research focuses on cultural factors that are the same in both mergers and acquisitions.
International merger and acquisition	Similar definition to that of a domestic M&A, except that the transaction involves transferring assets across country borders. IM&As fall within the domain of foreign direct investment (FDI) theory (Hymer, 1960, 1976).
Success or failure	In the existing research, measured by the shareholder value of the buying firm, effective organizational restructuring, operating performance, employee commitment and cooperation, and turnover among acquired managers (Bruner, 2004). The present study measures success or failure by exploring whether the IM&A reached its objectives and its expected overall outcomes.
IM&A process	• Pre-implementation: planning, identification of a suitable company, appraisal or evaluation of the potential partner, negotiating and reaching agreement about a merger or acquisition. • Implementation: integration of the IM&A partners. • Post-implementation: sustainability or maintenance (Forstman, 1998, p. 90).
Corporate governance	One issue in the relationship between headquarters and a foreign subsidiary is the agency problem arising from possible conflicts of interest between ownership and managers. This conflict is mitigated through the economic and legal institutions that protect the rights of shareholders and stakeholders. Although an IM&A falls, "in theory, under the jurisdiction

	of two countries, in practice, neither of the two has complete control" (Kobrin, 2003, p. 187). The "ambiguity makes problematic the nationality of the subsidiary and raises questions about whose law applies" (Kobrin, p. 189). This conflict and discrepancy between the two judiciary systems of an IM&A operation relate more to legal issues; however, managers' acceptance and preferences make a difference in how they respond to them. This research focuses on this aspect of corporate governance: the degree of acceptance of governance from the cultural point of view.

Table 4: Cultural Factors and Corporate Governance

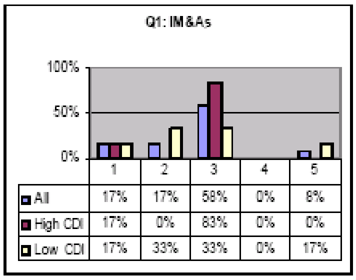
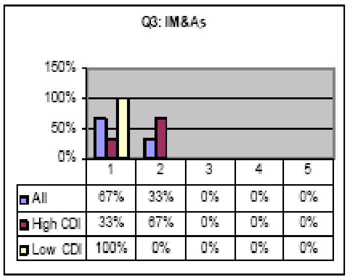
<table>
<tr><td>Question: To what extent do you agree with the following statement? Territory (and not ownership) should define a government's domain of control. A government's interventions should be limited to business operations in its own territory.</td><td rowspan="2">
</td></tr>
<tr><td>Ranking: High CDI responses in IM&As show higher concentration at the center (83%), showing preference for balance of power between headquarters and subsidiary.
Low CDI responses in IM&As show lower concentration at the center (33%). The remaining responses are distributed at both ends of the spectrum, but more to the left (toward 1 and 2) (50%), reflecting a higher preference for control by territory.</td></tr>
<tr><td>Question: Do you agree that governments should work toward eliminating both overlapping regulations and gaps between their jurisdictions?</td><td rowspan="2">
</td></tr>
<tr><td>Ranking: Both high and low CDI respondents would prefer a smaller gap, but low CDIs are stronger in this preference (all LCD IM&As are ranked number 1)</td></tr>
</table>

Table 5: Double Identity and Cultural Adaptation

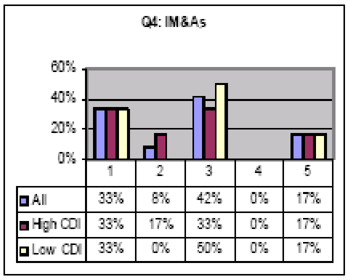
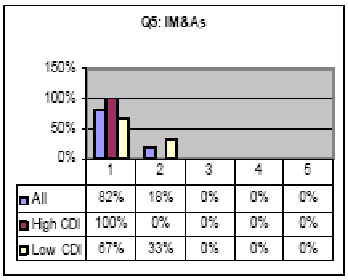
<table>
<tr><td>Question: To what extent do you agree that the subsidiary should adapt to the headquarters' culture to form a standard and unified corporate identity? To what extent has your subsidiary adapted to the headquarters' culture?</td><td rowspan="2">
</td></tr>
<tr><td>Ranking: IM&A respondents from high CDIs have a stronger preference for subsidiary adaptation to headquarters (17% + 33% = 50% to the left) than respondents from low CDIs (33% to the left)</td></tr>
<tr><td>Question: In your operations, to what extent do you believe that double identity (headquarters and subsidiary) exists and has created problems in relationships and strategic decisions? Have you experienced any manifestation of double identity (headquarters and subsidiary)? Please explain the situation, its consequences, and how you managed this conflict of identity.</td><td rowspan="2">
</td></tr>
<tr><td>Ranking: Double identity is stronger in high-CDI IM&As (100% rank 1) than in low-CDI IM&As (67% rank 1 and 33% rank 2).</td></tr>
</table>

Table 6: National and Organizational Cultures

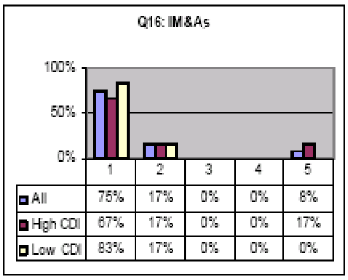
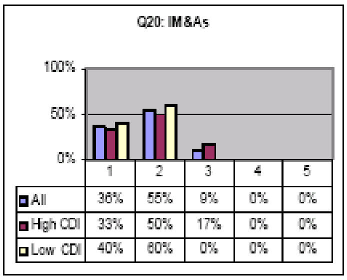
Question: In your interaction with other firms, have you seen common and recognizable characteristics among organizations of the same nationality? To what extent do you agree that firms of the same nationality have some common cultural factors that are recognizable and different from those of firms of other nationalities? Could you provide a few examples?	
Ranking: Distribution of responses from high and low CDIs are similar to some extent. Both groups are able to identify common characteristics among organizations from the same country.	
Question: Assuming that the two organizational cultures are compatible, to what extent do host country cultural compatibilities or differences affect foreign investors' investment decisions and IM&As' performance?	
Ranking: The difference between high and low CDIs is low. High CDIs are slightly to the center (17% at rank 3), while low CDIs are 100% to the left.	

Table 7: Cultural Factors in IM&As' Success

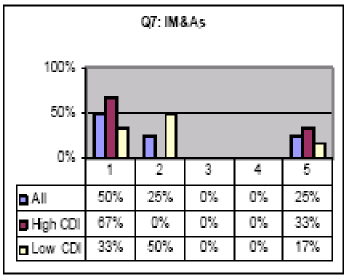
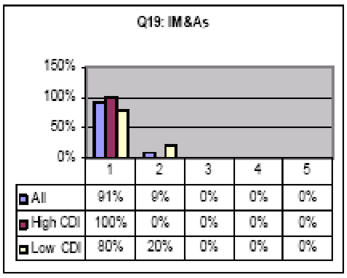
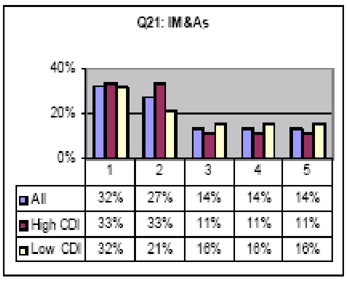
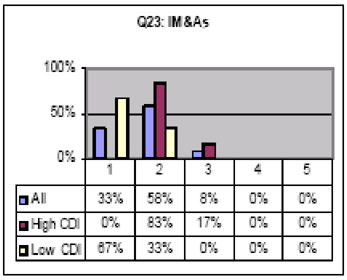
Question: To what extent do you agree that the objectives and expected outcomes of an IM&A should be clearly defined, understood, and shared before the implementation? To what extent were your objectives and expected outcomes defined and shared before implementation? Could you describe the original objectives and expected outcomes of your operations?	

Table 8: Cultural Factors in Phases of IM&As

Question: In IM&A due diligence, along with economic and financial factors, to what extent: (a) Did you account for cultural factors? (b) Do you think these factors should have been accounted for?	
Ranking: High CDIs have a stronger agreement (100% rank 1) than low CDI (80% rank 1) that cultural factors should be accounted for in IM&As due diligence.	
Question: In what phases were cultural differences more visible and disruptive? Please rank these phases in order of importance and provide a brief comment on why you consider one phase more important than the others.	
Ranking: There is no difference in the distribution of responses between high and low CDIs. The responses in both groups show the importance of cultural differences to have been greatest in phase 1, then less in phase 2, and least, but equal, for the remaining phases.	

Question: (a) Did you consider cultural factors in designing your IM&A's structure? (b) Should cultural factors, along with other factors, be considered in designing an IM&A's structure?

Ranking: High and low CDI responses are similar and clustered to the left.



Question: (a) Did you have (1) a strategy, (2) a plan to manage cultural differences? (b) Do you have (1) a strategy, (2) a plan to manage cultural differences for the next three or five years? (c) How important is it for foreign investors to have (1) a strategy, (2) a plan managing cultural differences?

Ranking: High and low CDI responses are similar and clustered to the left.

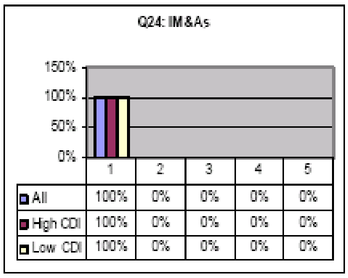
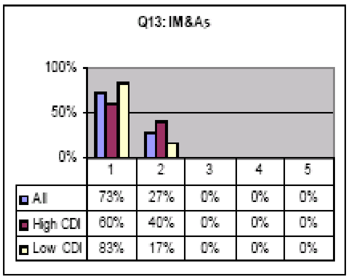


Table 9: Overall Effects of Cultural Factors in IM&As

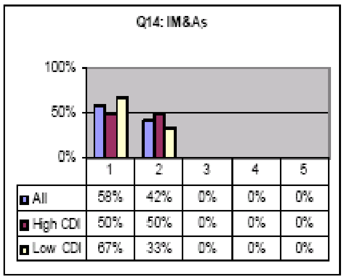
Question: To what extent do you agree that cultural factors of the host country have been among the major contributing factors (finance, technology, leadership) of your operations?

Ranking: Low CDI responses are more clustered at rank 1 (83%) than at rank 2 (17%).



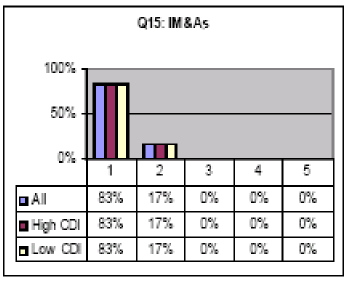
Question: Along with other contributing factors (finance, technology, leadership), how important will the cultural factors of the host country be in coming years?

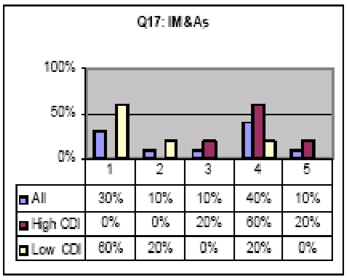
Ranking: The difference between high and low CDIs is in the degree of agreement. Low CDI responses are more clustered at rank 1 than rank 2. They are both 67% at rank 1.



Question: In your operations, to what extent do you think that cultural differences (or compatibility) between home and host countries are recognizable?

Ranking: High and low CDIs' responses have similar distribution and are clustered at rank 1.



<table>
<tr><td>Question: In your case, are cultural differences between home and host country complementary to the IM&A's objectives?</td><td rowspan="2">
</td></tr>
<tr><td>Ranking: There is a clear difference between the distributions of high and low CDIs. High CDIs of all responses are 80% clustered to the left. Low CDIs have the opposite distribution and are clustered 80% to the right.</td></tr>
</table>

About the Author

Dr. Mehdi Majidi

Mehdi Majidi is a principal consultant and a university faculty with more than 25 years experience in private and public management and international business. His key skills and knowledge lie in the areas of international business strategy, cross-cultural management, and engaging the private sector in socioeconomic development. Mr. Majidi is especially skilled in strategic planning and implementation of international mergers, acquisitions, and alliances. In this area, he focuses on cultural differences as a decisive factor in addition to financial and economic considerations. His consulting projects include industrial development, workforce development, implementation of information technology in education, and the design of a solution to measure, monitor, and evaluate the dynamics of the socioeconomic progress of a country based on international standards indexes. He has consulted for the U.S. Agency for International Development (USAID), the U.S. Department of Defense (DoD), the U.S. Department of Education (ED), and the World Bank. Mehdi Majidi is also a university faculty member, designing and teaching graduate level courses in international business strategy and cross-cultural management. He designs and provides executive training workshops and presentations and serves on academic panels. He has worked in different countries and speaks several languages.

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