

What We Know about M&A Success

A Research Agenda for the Lodging Industry

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The lodging industry is a fruitful area for merger and acquisition (M&A) research, although the empirical evidence is surprisingly sparse given the degree of industry consolidation. Although the M&As are motivated by the expected synergy between the target and the acquiring firms, some mergers are successful while others are not. Studies have found that, on average, lodging transactions are distinct from those in other industries because owners of both target and acquirer are better off after the merger. A thorough analysis of lodging M&A deals may enhance our knowledge of the factors related to successful deals not only in the lodging industry but also in other industries. This investigation of the current state of knowledge of M&A success suggests an agenda for further research on lodging industry transactions. In particular, identification of the best practices associated with each stage of the M&A process, especially about how lodging firms integrate, transfer, and manage the resources of the combined firm, is a ripe area for future research.

Keywords: mergers and acquisitions; lodging industry mergers; synergy; integration

The economic significance of merger and acquisition (M&A) transactions in the lodging industry is substantial, especially considering the 4,966 deals announced from the beginning of 1981 through August 1, 2009, with a total target value of \$601 billion and an average target value of \$121 million. Managers involved in M&A deals in all industries commonly cite the benefits of various sources of synergy from the merged operations. However, dispassionate analysis finds a discrepancy between managers' claims of added value and the actual outcome. Summarizing studies on M&As, Jensen and Ruback (1983), for example, concluded that mergers' added value accrues entirely to the companies that are bought out, while the acquiring shareholders at best break even. Although a more recent

study found that lodging industry mergers are successful on average (Canina 2001), meaning that the merger creates value for both parties, most subsequent studies have underscored Jensen and Ruback's findings.

In this article we review and summarize the research on M&A (notably, its antecedents and salient factors) with focus on the directions for lodging M&A research. We consider why some mergers are successful while others are not, based on a wide-ranging review of M&A studies. We conclude with questions for future research.

Defining Merger Success

We see two different definitions of merger success. A classic finance approach defines a successful merger as one in which the postmerger value of the integrated firm is higher than the sum of the acquisition price paid for the target firm and the value of the acquiring firm prior to the merger (for example, Brealey, Myers, and Allen 2005, 826). Under this approach, a successful merger or acquisition is one in which the value of the combined firm exceeds the cost of the total investment.

The financial market sees the matter differently. The market typically defines a successful merger as one where the value of the combined firm exceeds the sum of the values of the separate entities before they were merged. As viewed by the financial market, the total synergy value resulting from a merger equals the difference between the combined firm value and the sum of the initial values of each individual firm.

The difference between these two definitions of merger success can be considerable, because the acquisition price frequently exceeds the market's valuation of the target firm, due to the additional premium paid to shareholders of the firm that is

being absorbed. The acquisition price per share in many cases is 40 to 60 percent higher than the actual share price (Moeller, Schlingemann, and Stulz 2005). The premium given to the shareholders of the target firm can be viewed as an incentive for them to part with their existing stock (and the future value of its dividends and appreciation). The acquiring company is willing to pay this requested premium to shareholders since managers expect a much greater return based on synergy resulting from the merger. Thus, if we redefine the price paid for the target firm as the value of that firm plus a price premium, then a successful merger or acquisition is one in which the net gain to the acquirer, as represented by the net present value of the total synergy less the price premium, is greater than zero.

Regardless of the definition of merger success, the realization of the synergy through successful integration is essential to create value. The sources of merger gains are revenue enhancement and cost savings (Houston, James, and Ryngaert 2001). When Doubletree merged with Promus in 1997, for instance, the Promus board considered that merger synergies would stem from the cross-selling of hotel brands, increases in the franchise sales of the Doubletree brands, cost reductions as a result of the integration of information systems and support functions, and the combined purchasing power of the two companies.¹ Hilton Hotels' management made similar arguments two years later when it acquired the merged Promus company.

The classic argument is based on the revenue enhancement to be attained through improved management, on the assumption that the management of the acquiring firm is superior to that of the target firm (Manne 1965; Jensen and Ruback 1983). The cost savings are achieved if a more efficient

1. See the joint filing to the Securities and Exchange Commission, <http://www.sec.gov/Archives/edgar/data/923472/0001047469-97-005056.txt>.

firm is created through the elimination of redundant facilities and personnel or through offering a more profitable mix of products and services. Also, increased market power may raise performance. While these rationales for value creation in mergers are used to justify M&A decisions, they are more related to the expected synergy. However, the premium that has to be paid is often not fully considered in M&A decisions.

Measuring Success

Finance researchers have considered both definitions of merger success and value creation in their studies. Three typical perspectives for measuring merger success are based on stock prices around the public announcement of the M&A, stock prices after merger completion, and operational performance after merger completion. From the financial market's perspective, abnormal stock returns around the merger announcement reflect how much shareholder value is created. One can then define success as a positive abnormal return, which is the key premise underlying the dominant methodology in the finance literature for studying M&As. Jensen and Ruback (1983) summarize the early studies that exemplify this methodology, while Andrade, Mitchell, and Stafford (2001) summarize more recent studies. The abnormal-return approach assesses a merger's success at the time of the announcement, based on stock price changes around the merger announcement that exceed the expected changes. Therefore, such an estimate can be made available as early as the announcement date. Because this measure incorporates all available information about the merger's prospective success, it reflects the financial market's expectation of whether the merger will succeed in creating value. The assumption here is that the financial market is efficient and that stock price

changes should take into account all information available about the merger at the time of announcement, including the synergy the merger can create. The drawback to that approach is that the information relevant to a merger's success might not be incorporated into stock prices efficiently at the time of the announcement, especially given the complexity of merger deals. A particular source of distortion is managerial optimism based on past performance of "glamour" acquirers, which are firms with high past sales, asset growth, and returns. For example, Rau and Vermaelen (1998) find that acquirers of glamour firms tend to underperform in the postacquisition period.

To partially alleviate the reliance on market efficiency (at the time of the merger), researchers have also investigated long-run stock performance of merged firms (see Agrawal and Jaffe 2000). We note a heated debate on methodologies for measuring long-run returns. Moreover, the chief purpose of such studies is to test the information-processing efficiency of financial markets. However, these studies can also be used to define merger success or failure. One definition of a failed merger would be if the merged firm's stock incurs negative abnormal returns for a reasonable time period after deal completion (usually three to five years). The definition of a successful merger would be the opposite: three to five years of abnormal positive returns. A direct benefit of this approach is that it considers the unexpected portion of the merger information using stock price data following a deal's completion. Because this measure is only available three or more years after deal completion, it is not directly relevant for managerial decision making at the time of a merger announcement or negotiation. However, studies that relate the long-run postmerger performance to premerger firm and deal characteristics still provide helpful clues for managers

and investors of merging companies. For example, Rau and Vermaelen (1998) find that postmerger performance is negatively related to prior performance, Loughran and Vijh (1997) find stock-financed and negotiated mergers underperform in the long run, and Louis (2004) reports that acquirer underperformance is related to predeal earnings management.

From an operational perspective, merger success is defined by operational performance that is improved compared to that before the merger. Taking this approach, for example, Healy, Palepu, and Ruback (1992) found improved operational performance, measured by pretax cash flow on assets, for their sample of large deals. However, from the shareholders' perspective, the operational performance improvement after a deal's completion is only part of the merger gains. The rest of the gain is in stock appreciation. Any improved cash flow returns represent only an incomplete and indirect measure of shareholder value creation in mergers. We say this because cash-flow improvement is measured only for the year at hand, unlike stock prices, which are forward-looking and take into account future cash flows.

Current State of Knowledge

The overall evidence indicates lack of success on average for shareholders of the acquiring firm, even though it appears that M&As do create value on average. The average results, however, mask the substantial variation in merger performance. Rich evidence shows that various firm, deal, and market characteristics, together with their interactions, affect merger success. Exhibit 1 presents a brief summary of this literature.

The empirical results are more or less consistent regardless of whether one analyzes a deal based on announcement-period abnormal returns, long-term stock returns, or measures of operating performance. The announcement period abnormal return is the

most frequently used measure (King et al. 2004). As we noted above, one of the most striking but persistent findings throughout this literature is that target firms typically experience large significant abnormal returns at the deal announcements, while shareholders of acquiring firms on average do not gain from the mergers. Acquirers' abnormal returns around announcements are either insignificantly different from zero (Andrade, Mitchell, and Stafford 2001) or even negative (Bhagat et al. 2005; Betton, Eckbo, and Thorburn 2009; Bouwman, Fuller, and Nain 2009; Bradley and Sundaram 2006; Dong et al. 2006; Hackbarth and Morellec 2008; Moeller, Schlingemann, and Stulz 2007; Officer 2003, 2004). That said, the combined returns are usually positive and significant (Andrade, Mitchell, and Stafford 2001; Jarrell, Brickley, and Netter 1988; Jensen and Ruback 1983). The overall evidence suggests that mergers do create value, even if the gains accrue entirely to target shareholders (Andrade, Mitchell, and Stafford 2001).

The status of acquirer shareholders becomes even more puzzling in some cases when long-run stock returns are used as the performance measure. Long-run abnormal returns are at best insignificantly different from zero in all studies, even using different measurement methods. Some studies report significantly negative results (Betton, Eckbo, and Thorburn 2008; Bouwman, Fuller, and Nain 2009), indicating that M&As are not beneficial from the long-run shareholders' point of view. Others find that the acquirers' long-run abnormal returns are insignificantly different from zero (Mitchell and Stafford 2000; Betton, Eckbo, and Thorburn 2008) or significantly negative for the equal-weighted portfolio and insignificant for the value-weighted portfolio (Andrade, Mitchell, and Stafford 2001).

The findings are mixed when postmerger operating performance is examined. Healy,

Exhibit 1:

Factors Associated with Merger and Acquisition (M&A) Performance

<i>Factor</i>	<i>Type</i>	<i>The Impact on the M&A Outcome</i>	<i>Related Analytical Framework</i>
Deal characteristics			
Method of payment	Cash	+	Signaling of the bidder stock valuation
Type of deal	Stock	-	Agency theory; market for corporate control
	Tender offer	+	
Firm characteristics			
Managerial self-interest	High agency problem (high free cash flow, bigger size, overconfident managers)	-	Agency theory
Target firm's private/public status	Private target	+	Private firm discount
M&A experience	Experienced acquirer	+	Organizational learning
Relatedness	Inexperienced acquirer	-	Resource-based theory of firm
	Related	+	
Similarity	Conglomerate	-	Organizational learning
	High similarity	+	
State of stock valuation	Low similarity	-	Performance extrapolation hypothesis; long-run stock price reversion
	Low book to market/ overvaluation of stock	-	
Environmental			
Overall conditions of the financial market	High-valuation market	-	Agency theory
Merger wave	Low-valuation market	+	Managerial herding
	First movers in the wave	+	
	Follower in the wave	-	

Palepu, and Ruback (1992) document significant improvements in asset productivity and operating cash flow returns relative to a control group for a sample of the fifty

largest U.S. mergers between 1979 and mid-1984. They conclude that the underlying equity revaluations for the merging firm are based on the expectations of the real

economic gain from the acquisition rather than a mere wealth redistribution between the target and the acquirer. Andrade, Mitchell, and Stafford (2001) find similar results, but recently Bouwman, Fuller, and Nain (2009) reported significant negative abnormal returns on operating income for merged firms.

Deal Characteristics

Mergers differ from each other in many characteristics, such as the method of payment (stock vs. cash), deal type (tender offers vs. mergers), firm sizes, relative size, and parties' attitudes. Perhaps the two most critical issues are the method of payment and deal type.

Method of payment. While various factors affect the method of payment,² a widely examined rationale is that of signaling. Acquirers that use stock to finance acquisitions signal to the market that their shares are overvalued (Myers and Majluf 1984). As a result, the market will reevaluate the acquirer shares downward at the announcement of mergers, leading to negative abnormal returns. This intuition is strongly confirmed in a large body of empirical studies based on announcement-period abnormal returns to acquiring firms (Andrade, Mitchell, and Stafford 2001; Betton and Eckbo 2008; Bouwman, Fuller, and Nain 2009; Carow, Heron, and Saxton 2004; Huang and Walkling 1987). By contrast, a significantly positive announcement return was found for cash-financed acquisitions of large public targets (Fuller, Netter, and Stegemoller 2002) and for cash-financed acquisitions by small public bidders for public targets (Betton, Eckbo, and Thorburn 2008).

The method of payment appears to affect long-run returns as well. For example, Rau

and Vermaelen (1998) found that acquirers making stock acquisitions underperform those using cash, as did Loughran and Vijh (1997).

In terms of the operating-performance measures, no significant relationship between the payment type and the postacquisition operating performance is found (Healy, Palepu, and Ruback 1992; Heron and Lie 2002). In contrast, Bouwman, Fuller, and Nain (2009) report significantly negative abnormal operating income for the stock-financed deals and insignificant abnormal operating income for the cash-financed deals.

Tender offer versus merger. Agency theory proposes that M&As are a means to protect shareholders (of target companies) from existing poor management (Jensen 1986; Jensen and Ruback 1983). This implies the existence of a market for corporate control in which ineffectively managed firms are takeover targets and managers of those acquired firms are subject to turnover. Thus, as shown in Exhibit 1, a tender offer, in which the acquirer approaches the target shareholders directly and attempts to replace the incumbent managers of the target, is expected to perform better than a management-negotiated merger. Consistent with this notion, some studies showed superior performance for tender offers relative to mergers at the announcement date (Bouwman, Fuller, and Nain 2009; Jensen and Ruback 1983; Betton, Eckbo, and Thorburn 2008), but these results are not consistent across studies. Bhagat et al. (2005) report nonsignificant announcement abnormal returns for the acquirers involved in tender offers. Similarly, Huang and Walkling (1987) find no significant difference in the announcement abnormal returns between tender offers and mergers after controlling for payment method and

2. For example, tender offers tend to use cash, cash-rich acquirers tend to use cash, and acquirer managers with large ownership stake prefer cash to avoid dilution. See Martin (1996).

degree of resistance. The long-term results seem to confirm the value creation of tender offers over mergers. The long-run abnormal stock return for tender offers is positive, while for mergers it is negative (Rau and Vermaelen 1998). Using the data for mergers only (not tender offers), where the postacquisition underperformance is more prevalent, Agrawal, Jaffe, and Mandelker (1992) find that shareholders of acquirers experience a statistically significant loss over the five years following the merger.

Loughran and Vijh (1997) extended these studies by analyzing the impact of both the payment method, cash versus stock, as well as the type of deal, tender offer versus merger. They document that the long-term buy-and-hold excess returns are significantly positive for cash-financed tender offers and significantly negative for stock-financed mergers.

Bouwman, Fuller, and Nain (2009) also examined the impact of the deal type in combination with the payment method. However, their result is different from other studies, as follows. They reported that regardless of the deal type (merger or tender offer), the stock-financed deals resulted in significantly negative results, while cash-financed deals showed non-significant result for all the performance measures (announcement return, long-run buy-and-hold return, and operating performance).

Firm Characteristics

Private versus public. It is well documented that private target firms are acquired at a substantial discount relative to equivalent public firms. This may be explained by the relative illiquidity or severe information asymmetry between the private company owners and the acquiring firms (Chang 1998; Fuller, Netter, and

Stegemoller 2002). As a result, acquirers of private targets experience relatively superior abnormal returns (Betton, Eckbo, and Thorburn 2008; Capron and Shen 2007; Chang 1998; Fuller, Netter, and Stegemoller 2002).

The information asymmetry hypothesis is reconfirmed in a recent study by Cooney, Moeller, and Stegemoller (2009). They used a sample of private target firms that withdrew an initial public offering, which means their valuation histories are available. In addition to the positive announcement return for the acquirer, which is consistent with other studies with private targets, Cooney, Moeller, and Stegemoller find a positive relationship between the acquirer's announcement return and the target's value revision, which is measured by the difference between the value of the target at the time of its planned initial public offering (IPO) and the acquisition price. Because of information asymmetry, a larger revision of firm value reflected in the acquisition price signals greater value of the private firm, leading to greater gains to the acquirers. With regard to private acquirers, Barger et al. (2008) find that private equity acquirers pay lower premiums to publicly traded targets. The evidence is consistent with the fact that acquirers that are operating public firms pay more because they expect to realize synergy gains from the acquisitions, while for private equity acquirers the expected synergy is much lower.

The literature also finds that acquirer returns are affected by the interaction between the public status of the target, size of the target, and the form of payment. For example, stock-financed acquisitions of large public firms lead to lower (more negative) acquirer abnormal returns, while acquirers of stock-financed acquisitions of large private firms earn higher abnormal returns.

Managerial behavioral bias. When managers are influenced by hubris, they tend to make acquisitions that destroy value (Roll 1986). Malmendier and Tate (2008) report that overconfident managers are more likely to undertake acquisitions, especially engaging in diversifying deals that do not require external financing.

Managerial self interest. Since the Jensen and Meckling study (1976), agency problems between corporate managers and their shareholders are well understood. This study's direct implication in the M&A context is that acquirer shareholders earn lower abnormal returns when the agency problems with the acquirers are more severe.

Jensen (1986) argues that managers endowed with free cash flows will invest in projects having a negative net present value. Consistent with this hypothesis, there is a negative relationship between acquirers' abnormal returns and the level of their free cash flows (Lang, Stulz, and Walkling 1991; Harford 1999).

Grinstein and Hribar (2004) find that acquirer abnormal returns are lower when the acquiring CEOs have a higher degree of managerial power. Harford and Li (2007) argue that corporate governance plays an important role in monitoring the agency problem. Using buy-and-hold abnormal returns of acquirers' stock, they present evidence that even in mergers where bidding shareholders are worse off, bidding CEOs are better off three-quarters of the time, supporting the possibility that managers' self-interest may influence M&A activity. They also report that the monitoring role of the board is important. In the presence of a stronger board, CEO salaries are reduced as a result of negative acquisition-related performance.

Firm size is often used as another proxy for the agency problem. The announcement abnormal return is significantly higher for small acquirers than for large acquirers (Moeller, Schlingemann, and Stulz 2004).

Using accounting measures, Harford (1999) finds that mergers by the cash-rich acquirers, indicating potential agency problems, are followed by abnormal declines in operating performance, as measured by the cash flow return to assets.

One way to mitigate agency problems is to align managers' compensation package to the stock value. Consistent with this notion, Datta, Iskandar-Datta, and Raman (2001) document a strong positive relationship between the acquiring managers' equity-based compensation and stock price performance around and following the acquisition announcement, as well as the long-run buy-and-hold abnormal returns.

Asset relatedness. The realization of synergy is affected by the actual combination of the resources through the merger (Barney 1988; Chatterjee 1986; King et al. 2004; Singh and Montgomery 1987). Many studies support the idea that horizontal mergers are more valuable than conglomerate mergers, because it is easier to realize expected synergies in horizontal mergers (Chatterjee 1986; Finkelstein and Halebian 2002; Morck, Shleifer, and Vishny 1990; Singh and Montgomery 1987). For horizontal mergers, researchers note that resource complementarity between the target and the acquirer, which Wang and Zajac (2007) define as the resources that are different but mutually supportive, is an important antecedent of acquisition performance (J. Kim and Finkelstein 2009). The degree of relatedness improves the operating performance of the acquirer (Healy, Palepu, and Ruback 1992). In addition, the sources of gains in horizontal mergers appear to come from improved productivity efficiency and buying power (Fee and Thomas 2004).

The similarity between the target's and the acquirer's organizational culture and management style affects the transfer of functional skills between the businesses (Salter and Weinhold 1978; Singh and Montgomery 1987). Thus, the impact of

similarity on M&A performance has been the subject of research. Empirically, higher differences in the management style between the target and the acquirer are associated with negative acquisition performance (Datta 1991; Chatterjee et al. 1992).

International deals may also be viewed in terms of (lack of) similarity. International mergers involve nation-specific differences in addition to firm-specific differences (Olie 1994). Consequently, international acquisitions are associated with inferior performance relative to domestic ones (Eckbo and Thorburn 2000; Moeller and Schlingemann 2005).

Acquisition experience. Although organizational learning theory predicts that an acquirer's acquisition experience will influence performance in subsequent acquisitions, the empirical results are mixed. While Fowler and Schmidt (1989) report that long-term stock returns improve significantly for acquirers that have previous acquisition experience, Lubatkin (1983) and Ravenscraft and Scherer (1987) find no such effect. Bruton, Oviatt, and White (1994) document a positive relationship between the acquirer's previous experience and acquisition performance measured by return on sales for financially distressed targets, but they find no effect with nondistressed targets.

Haleblian and Finkelstein (1999) hypothesize that acquirers start out by making generalization errors that diminish M&A performance until they develop a sufficient amount of experience. Consistent with this proposition, they find an overall U-shaped relationship between an organization's acquisition experience and its acquisition performance as measured by the announcement abnormal returns and accounting returns (return on assets, or ROA). Zollo and Singh (2004) expand this study by proposing that experience alone does not improve the long-run acquisition performance, while knowledge codification strongly does so.

Past performance. Rau and Vermaelen (1998) argue that the long-term underperformance of acquiring firms in mergers is predominantly caused by the poor postacquisition performance of low book-to-market "glamour" firms. They explain this phenomenon by the possible overextrapolation of bidders' past performance into the future. However, Andrade, Mitchell, and Stafford (2001) found insignificant long-term stock performance for both glamour and value firms.

Financial market influence. The merger waves of the 1960s and 1990s occurred during periods of high stock market valuation, while 1980s mergers coincided with low valuation (Shleifer and Vishny 2003). Researchers find that M&A outcomes differ as a result of the valuation differences in the overall financial market (Bouwman, Fuller, and Nain 2009; Rhodes-Kropf, Robinson, and Viswanathan 2005) as opposed to the firm-specific valuation levels (market-to-book ratio) as in Ang and Cheng (2006), Dong et al. (2006), and Rau and Vermaelen (1998).

In an empirical study, Bouwman, Fuller, and Nain (2009) report that the acquirer's abnormal announcement returns are insignificantly negative during a booming market and significantly negative during the market trough. In the long term, however, the pattern is reversed: lower in the high-valuation market and higher in the lower-valuation market. In addition, the operating performance is also worse for acquisitions made in the high-valuation market, suggesting that the long-run underperformance of the high-market acquisitions is not just a result of the long-term stock price reversal. These results suggest the strong influence of financial markets on acquisition success.

Some scholars suggest that merger waves may occur due to herding behavior of managers, although the shock that initiates the first merger in the wave may be purely idiosyncratic (Goel and Thakor 2008). This

hypothesis, which predicts that the performance of the followers in the merger wave is worse than that of the first movers, found support from McNamara, Haleblian, and Dykes (2008) and Goel and Thakor (2008). Similarly, Bouwman, Fuller, and Nain (2009) note that not all acquisitions undertaken during a high market underperform. Early movers do not destroy shareholder value, and the earliest movers actually create shareholder wealth, while for the late movers value is destroyed.

Moeller, Schlingemann, and Stulz (2005) note a small number of acquisitions with an extremely large loss in terms of the dollar return between 1999 and 2001, the largest merger wave in the United States. They observe that the firms that realized large acquisition losses earned positive abnormal returns prior to the year of the acquisition but significantly lower abnormal returns during the year following the acquisition. They propose that the high abnormal returns prior to the merger allowed managers greater discretion that, in turn, resulted in poor acquisition decisions.

Integration Process

Our discussion has employed the typical M&A division into three stages: the premerger process, the actual deal, and postmerger integration. The most accurate estimation of the potential value creation and the firm's ability to capture the value involves a thorough analysis during each stage of the M&A process and a plan for managing each of the stages. The final outcome of the M&A is the result of the success of premerger decision making plus the success of postmerger implementation (Pablo 1994). Managers often view the premerger and postmerger processes as separate issues (Tetenbaum 1999; Chanmugam et al. 2005). Many companies do not plan the integration process until after the deal is announced or even closed (Carr et al.

2005), which is too late. Often different groups and even different managers are involved in the predeal and postdeal stages. This may result in a disconnection between the expected benefits of the M&A and the achievement of those benefits. Thus, to achieve the desired synergy, managers need to incorporate the integration plan early on based on the identification of the areas where integration is important, the degree of integration, and the synergy expected.

Scholars have also analyzed M&A from this perspective (Capron 1999; Jemison and Sitkin 1986; Haspeslagh and Jemison 1991; Larsson and Finkelstein 1999; Zollo and Singh 2004). This stream of research emphasizes the importance of the integration process for synergy realization, noting that all value creation actually takes place after the acquisition (Haspeslagh and Jemison 1991). The integration design and the management of the M&A process are essential to the success or failure of an acquisition (Pablo 1994).

In creating a new corporate entity, mergers disrupt existing balances through the removal and addition of corporate functions. The modification alters revenue, turnover, and profit, which are directly related to the interaction of the groups of activities within the corporate system (Puranam, Singh, and Zollo 2003). To identify and realize synergies, managers must understand the strengths and weaknesses of both firms' business processes and combine those resources in a novel way. The unification of the business processes to maximize value and synergy requires viewing the combined corporation as a new system that will drive the valuation of the combined firm.

One of the first studies in this stream of research is that of Capron (1999), who showed that postacquisition asset divestiture and resource redeployment contribute to acquisition performance. However, Capron also identified a significant risk of damaging performance when the divested

assets and redeployed resources are those of the target.

Birkinshaw, Bresman, and Håkanson (2000) suggest that the integration stage involves two processes, namely, human integration and task integration. Their key observation is that the human integration process facilitates the effectiveness of the task integration. Thus, a low level of human integration will limit the effectiveness of task integration as a driver of acquisition success. Cording, Christmann, and King (2008) applied four dimensions of integration decisions (i.e., integration depth, integration speed, top management turnover, and market focus) as they affected two intermediate goals (internal reorganization and market expansion).

With respect to the integration speed, Homburg and Bucerius (2006) examined a sample of horizontal mergers and showed that speed is most beneficial when external relatedness (e.g., target market and market positioning) is low and at the same time internal relatedness (e.g., organizational culture) is high; in contrast, speed is highly detrimental in the case of low internal and high external relatedness.

Zollo and Singh (2004) emphasize the codification of the M&A experience rather than the experience per se. As a measure of codification, they investigate whether the acquirer has developed documents or manuals or quantitative models. Using a sample of the U.S. banking industry, they find that knowledge codification strongly and positively influences ROA, while experience accumulation does not.

Merger and Acquisitions in the Lodging Industry

From January 1, 1981, through August 1, 2009, lodging industry mergers and acquisitions involved target companies based in 112 nations and acquiring companies based in 105 nations (see Exhibit 2). The data

sample, supplied by Securities Data Corporation (SDC), includes M&As of both public and private companies in which at least one of the companies involved operates in the lodging industry.

As shown in Exhibit 2, lodging M&A has seen a cyclical pattern. While lodging M&A generally moved parallel to the global financial market conditions, industry-specific factors have had a strong effect. In the mid-1980s, for instance, lodging and other commercial real estate development in the United States was distorted by favorable tax laws, which encouraged development and mergers. Partially as a result of those laws, Exhibit 2 shows higher total and average value of the deals in the period of 1984 to 1986 than in the earlier period. Although the general market condition in the United States deteriorated in the late 1980s, the annual value of the targets exceeded \$10 billion for the first time in 1988 and 1989, reaching \$13 billion in each of these two years, influenced by the liberalization in the global financial investment (see Renaud 1997). Changes in tax laws altered the industry structure in the early 1990s, but an economic bubble and different tax loopholes subsequently drove the most dramatic M&A increase, which reached a peak in 1997 when the total value of the targets reached \$64 billion and involved 420 deals. The tax loopholes involved what was known as the paired-shared REIT (real estate investment trust). Starwood Lodging Trust, then a REIT, acquired ITT-Sheraton, defeating the competing hostile bid from Hilton, and Westin Hotels in 1997; and Patriot American Hospitality acquired Wyndham Corporation and InterState Hotels in 1997. With a distinct tax advantage awarded to their grandfathered paired-shared status, Starwood and Patriot American Hospitality accounted for 33 percent of the total transaction volume announced in 1997. In the following year, Meditrust Corporation,

Exhibit 2:
Summary Information on Mergers and Acquisitions (M&As) by Year, January 1, 1981, to August 1, 2009

Announcement Year	Number of M&As	Total Value of Targets (\$ Millions)	Mean Value of Targets (\$ Millions)	Percentage of Public		
				Domestic	Horizontal	Acquirer
						Target
1981	12	1,250.66	104.22	66.67	25.00	66.67
1982	7	279.65	39.95	71.43	28.57	42.86
1983	29	1,687.55	58.19	86.21	20.69	44.83
1984	27	3,816.23	141.34	85.19	14.81	44.44
1985	15	2,288.53	152.57	86.67	20.00	33.33
1986	28	5,588.93	199.60	71.43	32.14	46.43
1987	55	7,041.44	128.03	67.27	34.55	45.45
1988	108	13,202.34	122.24	73.15	35.19	53.70
1989	98	13,022.56	132.88	60.20	32.65	60.20
1990	91	8,955.61	98.41	50.55	31.87	46.15
1991	95	5,168.17	54.40	62.11	26.32	28.42
1992	94	6,059.52	64.46	53.19	23.40	39.36
1993	165	6,240.44	37.82	61.21	22.42	29.09
1994	216	9,913.69	45.90	65.74	32.87	51.39
1995	220	23,944.22	108.84	75.45	27.73	50.45
1996	300	29,124.62	97.08	82.00	32.33	62.00
1997	420	64,251.13	152.98	78.33	32.62	63.81
1998	325	30,739.92	94.58	76.62	33.54	51.38
1999	314	23,817.97	75.85	74.52	37.58	42.36
2000	255	21,870.41	85.77	69.80	26.67	41.57
2001	179	14,625.45	81.71	70.95	32.96	37.99
2002	203	17,741.74	87.40	74.38	25.62	34.98
2003	228	16,901.81	74.13	75.44	21.05	30.26
2004	224	37,344.40	166.72	74.11	26.34	33.48
2005	357	57,620.96	161.40	82.91	24.09	30.81
2006	329	79,499.64	241.64	77.20	18.84	43.77
2007	292	81,152.39	277.92	73.97	22.60	36.30
2008	202	15,074.97	74.63	72.77	23.27	22.77
2009	78	2,908.88	37.29	67.95	23.08	23.08
1981 to August 1, 2009	4,966	601,133.81	121.05	73.52	27.93	43.15

another REIT with the paired-shared status, acquired La Quinta Inns Inc. In the subsequent years, the “buying spree” by the paired-shared REITs tapered off when Congress closed the tax loophole and the U.S. economy slowed down (see *Dow Jones Business News* 1998).

M&A activities picked up again after 2001, with the real estate bubble created by excess liquidity. Private equity firms accounted for most of the large-scale deals in this decade. The Hilton-Blackstone transaction in 2007 (\$26 billion) was recorded as the largest lodging deal in history. Fairmont and Four Seasons Hotels also became the target of the private investment firms in the 2000s. The reason that private equity funds were better able to take advantage of the low interest rates that prevailed in this period is that they could make greater use of debt financing than publicly traded firms, which were placed under a tighter regulatory environment under the Sarbanes-Oxley legislation (Corgel 2008).

Exhibit 2 also shows that, in general, domestic transactions and conglomerate acquisitions are the most common lodging industry deal. The majority of targets are nonpublic firms. Exhibits 3 and 4 summarize the top fifty acquirers and the target nations. U.S. firms were by far the most active, followed by companies in the United Kingdom and Australia. These three major countries hosted 55 percent of the acquiring firms and 60 percent of the target firms.

According to K. Kim and Olsen (1999), the most important stated objective for lodging M&A was to accelerate the growth of their firms. We have found limited empirical evidence that lodging M&As are generally successful (Canina 2001; Yang, Qu, and Kim 2009). Analyzing deals from 1982 through 2000, coauthor Canina

(2001) reported significantly positive announcement-day abnormal returns for both lodging targets and acquirers, in contrast to the results discussed above for other industries. Similar to the general findings, that study found a positive and higher return for the target than for the acquirer. Positive abnormal returns are also observed when the sample is divided into mergers and tender offers. This implies that the positive abnormal returns for acquirers in the lodging industry are not driven by the positive abnormal returns associated with tender offers. With more recent data, from the period of 1996 to 2007, Yang, Qu, and Kim (2009) also show that hospitality acquirers receive positive abnormal returns in the twelve months after an acquisition. These results support the notion that lodging mergers and acquisitions are value-enhancing. The results of other studies are conflicting, however. Hsu and Jang (2007) and Yang, Qu, and Kim (2009) found no exceptional positive outcomes for lodging deals.

Future Research for Hospitality

The lodging industry is a fruitful area for M&A research, although the empirical evidence is surprisingly sparse given the degree of industry consolidation. As of September 2009, the ten largest hotel companies controlled 59 percent of the total hotel rooms in the United States.³ At the same time, no single lodging company, including franchisors, account for more than 15 percent of hotel rooms in the United States.⁴

Hotel owners and operators have three main paths to growth: raise sales or profits at existing properties, open new units, or make acquisitions. A common rationale supporting the acquisition approach is that

3. “Major Lodging Companies—Rooms and Properties in the U.S.,” *H&MM*, September 2009, HotelWorldNetwork.com.

4. Standard and Poor’s *Lodging & Gaming Industry Survey*, May 21, 2009.

Exhibit 3: Summary Information on Mergers and Acquisitions (M&As) of the Top Fifty Acquirer Nations by Acquirer Nation, January 1, 1981, to August 1, 2009

Acquirer Nation	Number of M&As	Percentage of All	Total Value of Targets (\$ Millions)	Mean Value of Targets (\$ Millions)	Percentage of Public			
					Domestic	Horizontal	Acquirer	
United States	1,704	34.31	346,866.05	203.56	89.73	26.88	55.87	14.20
United Kingdom	647	13.03	85,728.54	132.50	82.53	41.27	49.30	9.89
Australia	375	7.55	22,813.97	60.84	94.67	24.00	38.93	13.87
Hong Kong	164	3.30	15,487.90	94.44	44.51	39.63	51.22	20.73
Singapore	161	3.24	12,273.23	76.23	41.61	22.98	43.48	27.33
Spain	159	3.20	8,779.11	55.21	74.84	54.72	18.24	10.69
Canada	137	2.76	14,826.00	108.22	74.45	27.01	67.15	7.30
Japan	137	2.76	11,076.56	80.85	70.80	15.33	38.69	11.68
France	114	2.30	15,534.18	136.26	68.42	32.46	56.14	32.46
Malaysia	91	1.83	4,023.31	44.21	73.63	15.38	45.05	19.78
Thailand	71	1.43	1,148.87	16.18	90.14	25.35	54.93	30.99
India	58	1.17	873.87	15.07	89.66	48.28	27.59	22.41
Sweden	53	1.07	3,029.73	57.16	67.92	54.72	60.38	18.87
China	47	0.95	1,191.62	25.35	80.85	12.77	36.17	23.40
Ireland-Rep	42	0.85	7,163.68	170.56	50.00	42.86	33.33	9.52
Italy	39	0.79	2,272.89	58.28	69.23	28.21	30.77	10.26
Norway	37	0.75	2,255.32	60.95	62.16	37.84	21.62	29.73
New Zealand	34	0.68	1,696.17	49.89	76.47	38.24	50.00	20.59
Netherlands	32	0.64	2,305.81	72.06	31.25	37.50	12.50	6.25
Bulgaria	32	0.64	102.74	3.21	96.88	21.88	9.38	3.13
Germany	26	0.52	2,697.40	103.75	57.69	11.54	23.08	3.85
South Africa	23	0.46	1,559.14	67.79	95.65	21.74	60.87	26.09
Portugal	22	0.44	856.22	38.92	77.27	31.82	4.55	31.82
Israel	20	0.40	2,755.38	137.77	60.00	30.00	45.00	20.00
Croatia	20	0.40	124.26	6.21	90.00	20.00	10.00	25.00

(continued)

Exhibit 3: (continued)

Acquirer Nation	Number of M&As	Percentage of All	Total Value of Targets (\$ Millions)	Mean Value of Targets (\$ Millions)	Percentage of Public			Target
					Domestic	Horizontal	Acquirer	
Belgium	19	0.38	1,052.98	55.42	42.11	31.58	42.11	52.63
United Arab Emirates	17	0.34	7,836.37	460.96	5.88	41.18	29.41	23.53
Switzerland	16	0.32	178.44	11.15	50.00	6.25	18.75	31.25
Hungary	15	0.30	291.83	19.46	73.33	40.00	66.67	20.00
South Korea	15	0.30	247.27	16.48	66.67	13.33	46.67	13.33
Finland	13	0.26	1,368.26	105.25	92.31	15.38	7.69	7.69
Bermuda	13	0.26	604.22	46.48	7.69	69.23	69.23	7.69
Greece	13	0.26	492.33	37.87	53.85	23.08	15.38	0.00
Austria	13	0.26	473.71	36.44	53.85	23.08	46.15	0.00
Philippines	12	0.24	339.79	28.32	91.67	16.67	58.33	33.33
Denmark	10	0.20	590.22	59.02	70.00	20.00	30.00	0.00
Russian Fed	10	0.20	568.58	56.86	60.00	40.00	0.00	0.00
Brazil	9	0.18	316.72	35.19	100.00	22.22	22.22	33.33
Mexico	8	0.16	1,973.62	246.70	87.50	37.50	37.50	25.00
Poland	8	0.16	177.47	22.18	100.00	25.00	37.50	0.00
Romania	8	0.16	46.00	5.75	87.50	12.50	12.50	12.50
Argentina	7	0.14	29.41	4.20	100.00	42.86	28.57	0.00
Indonesia	6	0.12	575.14	95.86	83.33	16.67	16.67	33.33
Bahamas	6	0.12	546.87	91.15	33.33	66.67	66.67	16.67
Egypt	6	0.12	353.84	58.97	100.00	33.33	16.67	16.67
Cayman Islands	5	0.10	382.75	76.55	0.00	0.00	40.00	60.00
Saudi Arabia	5	0.10	361.61	72.32	40.00	0.00	0.00	0.00
Kuwait	5	0.10	320.91	64.18	0.00	0.00	0.00	0.00
Taiwan	5	0.10	272.04	54.41	40.00	20.00	0.00	0.00
Morocco	5	0.10	98.50	19.70	100.00	40.00	20.00	0.00

Exhibit 4: Summary Information on Mergers and Acquisitions (M&As) of the Top Fifty Target Nations by Target Nation, January 1, 1981, to August 1, 2009

Target Nation	Number of M&As	Percentage of All	Total Value of Targets (\$ Millions)	Mean Value of Targets (\$ Millions)	Percentage of Public			
					Domestic	Horizontal	Acquirer	Target
United States	1,785	35.94	344,395.50	192.94	85.66	25.38	54.96	13.61
United Kingdom	672	13.53	95,999.11	142.86	79.46	38.54	43.30	8.93
Australia	565	11.38	29,783.36	52.71	62.83	20.88	29.03	12.39
Spain	155	3.12	7,751.72	50.01	76.77	43.87	17.42	7.10
Canada	147	2.96	16,138.30	109.78	69.39	26.53	56.46	10.20
France	126	2.54	15,533.75	123.28	61.90	27.78	44.44	26.98
Japan	111	2.24	7,016.19	63.21	87.39	11.71	37.84	18.02
Hong Kong	99	1.99	8,760.21	88.49	73.74	23.23	37.37	27.27
Singapore	94	1.89	8,751.82	93.10	71.28	24.47	50.00	52.13
Malaysia	85	1.71	4,242.45	49.91	78.82	15.29	44.71	17.65
Thailand	80	1.61	1,259.83	15.75	80.00	25.00	51.25	37.50
China	69	1.39	2,191.37	31.76	55.07	21.74	43.48	14.49
India	62	1.25	839.44	13.54	83.87	43.55	22.58	24.19
New Zealand	53	1.07	881.60	16.63	49.06	39.62	39.62	18.87
Italy	50	1.01	4,108.81	82.18	54.00	26.00	34.00	18.00
Sweden	49	0.99	4,529.06	92.43	73.47	51.02	59.18	20.41
Germany	44	0.89	5,208.54	118.38	34.09	36.36	25.00	2.27
Bulgaria	42	0.85	212.84	5.07	73.81	19.05	11.90	2.38
Netherlands	36	0.72	10,071.01	279.75	27.78	36.11	47.22	13.89
Norway	34	0.68	1,831.00	53.85	67.65	35.29	29.41	38.24
Ireland-Rep	33	0.66	3,568.62	108.14	63.64	27.27	30.30	12.12
Belgium	29	0.58	1,952.64	67.33	27.59	51.72	27.59	27.59
Portugal	27	0.54	1,036.47	38.39	62.96	29.63	3.70	22.22
South Africa	26	0.52	1,716.17	66.01	84.62	23.08	57.69	23.08
Croatia	24	0.48	355.70	14.82	75.00	20.83	16.67	16.67

(continued)

Exhibit 4: (continued)

Target Nation	Number of M&As	Percentage of All	Total Value of Targets (\$ Millions)	Mean Value of Targets (\$ Millions)	Percentage of Public			
					Domestic	Horizontal	Acquirer Target	
Mexico	24	0.48	2,766.27	115.26	29.17	29.17	45.83	8.33
Philippines	19	0.38	1,013.15	53.32	57.89	21.05	47.37	21.05
Finland	18	0.36	2,020.55	112.25	66.67	27.78	22.22	5.56
Poland	18	0.36	566.56	31.48	44.44	27.78	44.44	22.22
Argentina	17	0.34	108.82	6.40	41.18	41.18	29.41	0.00
Switzerland	17	0.34	820.45	48.26	47.06	23.53	41.18	17.65
Hungary	16	0.32	294.95	18.43	68.75	31.25	37.50	25.00
Brazil	15	0.30	740.94	49.40	60.00	46.67	33.33	20.00
Czech Republic	15	0.30	666.68	44.45	20.00	26.67	53.33	0.00
Morocco	15	0.30	186.56	12.44	33.33	26.67	33.33	0.00
South Korea	15	0.30	669.31	44.62	66.67	20.00	33.33	13.33
Austria	12	0.24	433.09	36.09	58.33	16.67	25.00	0.00
Greece	12	0.24	1,168.73	97.39	58.33	8.33	8.33	16.67
Indonesia	12	0.24	717.66	59.80	41.67	25.00	41.67	16.67
Israel	12	0.24	477.26	39.77	100.00	33.33	50.00	33.33
Romania	12	0.24	92.07	7.67	58.33	8.33	16.67	8.33
Russian Fed	11	0.22	314.07	28.55	54.55	36.36	27.27	0.00
Bahamas	10	0.20	3,770.02	377.00	20.00	70.00	20.00	30.00
Denmark	9	0.18	232.59	25.84	77.78	33.33	44.44	0.00
Puerto Rico	9	0.18	413.44	45.94	0.00	22.22	66.67	22.22
Cyprus	8	0.16	82.67	10.33	62.50	37.50	25.00	12.50
Kenya	8	0.16	44.93	5.62	37.50	25.00	12.50	0.00
Egypt	7	0.14	392.99	56.14	85.71	42.86	28.57	14.29
Estonia	7	0.14	44.16	6.31	28.57	14.29	28.57	28.57
Lithuania	7	0.14	39.89	5.70	57.14	14.29	14.29	0.00

it offers faster and possibly more economical growth than would new construction or refurbishing existing properties. If this is the case, we should expect that greater performance is realized as a result of an acquisition strategy relative to new development. This would be a fruitful area for future study.

A thorough analysis of lodging M&A deals may enhance our understanding of the factors related to successful deals not only in the lodging industry but also in other industries. Since the average success of bidding firms in the lodging industry differs from that of the overall market, further study of the strategies, objectives, motives, processes, methods, degree and choices of areas of integration, and other factors employed by lodging executives in M&A activity may increase the likelihood of successful outcomes for other industries. In particular, it would be worthwhile to investigate the factors that drive merger success (summarized in Exhibit 1). For example, a large percentage of lodging acquirers and targets are private firms. That might mean that the premium paid for the target is lower, and the acquirer enjoys relatively higher gains. This empirical question could easily be resolved.

As we discussed previously, the price paid for the target firm and prospects for synergy and integration influence directly the value realized by any merger. Given the extent of consolidation in the lodging industry, the large companies particularly have a significant amount of acquisition experience. Consequently, they may be better at valuation and at estimating and realizing synergies. Furthermore, because lodging companies can apply the most effective business models (including owning or franchising), large players operating multiple brands know the best way to integrate systems and processes.

This matter of integration is important because of the commonly held view that

the failure of mergers is related to inept integration. Following that idea through interviews with acquirers, Carr (2005) conclude that the following factors are important to add value, identify where to prioritize integration, quickly integrate the financial opportunities that inspired the deal, put cultural integration high on the agenda, and keep most of the employees' efforts on the base business. Though it is difficult, thoughtfully executed integration can magnify a deal's chances of success, especially given Haspeslagh and Jemison's (1991) pronouncement that "all value creation takes place after the acquisition." Future research for the lodging industry might take into account its highly differentiated market and the fact that firms manage, franchise, and own multiple segments both domestically and internationally. Consequently, the integration tasks may be similar to the tasks that they perform on a daily basis. Additionally, since the lodging industry is heavily invested in real estate, perhaps the degree of integration and ease of integration is significantly different from that found in other industries.

It is also possible that the finding of overall average success of lodging M&A reflects the results of deals involving the largest companies. It is feasible for large companies to realize economies of scale in their overhead expenses, for instance through augmented purchasing power. That kind of cost-cutting factor can give large companies a competitive advantage over smaller firms. In addition, companies with multiple brands or properties may have diversified their operations and risks.

Success in M&A deals depends both on the opportunity at hand and the process by which one manages it. The recognition of a strategic threat or opportunity in the firm's competitive environment motivates most deals. The industry positions of the buyer and target are important determinants of the attractiveness of a deal. Successful

acquirers must engage in an analysis of the strategic positions of the buyer and target. The ability to achieve a successful union of the two distinct organizations has an influence on the ability of the new firm to realize merger synergies and strategic benefits.

In summary, since the financial market views M&A in the lodging industry as successful for both the acquirer and target on average, we believe that the lodging industry is a fruitful industry to further pursue M&A research. In particular, the identification of the best practices associated with each stage of the M&A process, especially about how lodging firms integrate, transfer, and manage the resources of the combined firm, is a ripe area for future research.

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