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Mergers and acquisitions as value creation strategies

A study of major Finnish companies engaging in M&As

School of Marketing and
Communication
Master’s thesis in International
Business

Vaasa 2022

UNIVERSITY OF VAASA
School of Management
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Title of the Thesis: Mergers and acquisitions as value creation strategies : A study of major Finnish companies engaging in M&As
Degree: Master of Science in Economics and Business Administration
Programme: Master’s Degree in International Business
Supervisor: Tiina Leposky
Year: 2022 **Sivumäärä:** 68

ABSTRACT:

Popularity of mergers and acquisitions has grown, and they are increasingly used to seek growth and access routes to new market areas. Even though mergers and acquisitions represent a key cornerstone for companies to enhance operations, research regarding the subject is fragmented and results sometimes contradictory. Even though most of mergers and acquisitions fail to reach targets set prior, some companies appear to be more skilled in utilising M&As than others. Skillful executives can utilise imperfections of market valuations to benefit from too positive or negative valuation levels.

This thesis examines if companies can utilize mergers and acquisitions to create value for their shareholders. Data is collected to measure how merger and acquisition announcements influence stock prices of companies engaging in them. This data is then compared with a suitable benchmark to measure if value has been created. The chosen benchmark is the OMX25 Helsinki index, which represents stock price progression of the biggest and mostly traded Finnish companies in Helsinki stock exchange. There has been little research in value creation of mergers and acquisitions of Finnish companies, and this thesis aims to fill that void.

The empirical part of this research is conducted by using a quantitative analysis, while utilising time frame setting which is popular in event study method. Event study method remains a favoured and widely used method when measuring performance following major announcements, such as M&A news being published. As such, this this thesis examines stock price progression over a period of one month, with special emphasis placed on the first and fifth trading days of chosen time frame. Hypotheses are set to measure if companies can create value for their shareholders over chosen time frame.

The study finds that companies can create value for their shareholders. However, the results suggest that value is only created once, on the announcement day, after which value starts to be destroyed. This may be linked to transitory imperfections in market valuation levels due to risen volatility following the M&A announcement. Nonetheless, results are glaring, and shareholders can use M&A announcements to realize substantial profits. As such, shareholders are recommended to take an active stance with their shares if they are seeking to maximize their short-term profit.

KEYWORDS: mergers and acquisitions, value creation, announcement day, stock performance, market reaction

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1 Introduction

The purpose of this section is to give theoretical background on mergers and acquisitions (M&As), with special emphasis placed on using M&As to create value for shareholders. To illustrate the phenomenon further, real life cases are presented.

1.1 Research background

M&As have become increasingly significant and popular strategy in various business segments and geographical locations (Weber & Drori 2011). Companies engage in M&A activities to create value for their shareholders (Colman & Lunnan 2011). According to Birkinshaw, Bresman & Håkanson (2000), increased value can be achieved by creating mutual M&A targets. Colman & Lunnan (2011) extend this notion by mentioning that acquisitions alter and stretch organizational boundaries, which, in some cases, presents a threat for pre-acquisition identity. It has been proven that high resistance for change correlates with high failure numbers in change implementation. In addition, resistance for change among the employees was lower when they felt respected and had strong human relationships within their division. Furthermore, people-orientated values have been found to be helpful in implementing changes. (Jones, Jimmieson & Griffiths 2005; Harper & Utley 2001)

In addition to mergers and acquisitions, companies may use divestments to change their strategical direction. For example, historical key market areas for Fazer Group have been sweets, pastries and restaurant business. However, Fazer has recently undergone a strategical change, and sold its whole restaurant business, known as Fazer Food Services, in June 2019. CEO of Fazer commented that they will use these funds to support their growth strategy in other business segments (Helsingin Sanomat 2019). To illustrate, Fazer has acquired two significant companies producing oat-based groceries, Bioferme and Kaslink (Helsingin Sanomat 2019b). In another interview, Fazer states that they are aiming to challenge Oatly to become a major player in oat-based groceries business, which is growing rapidly (Helsingin Sanomat 2018).

Another Finnish company, Nokia, acquired 10 companies between January 2015 and May 2018. All these companies have been deemed to possess "interesting new technologies and competencies", which help Nokia to achieve its target in creating a mobile world (Nokia 2019).

Even if the core competences remain the same, Finnish companies must utilize abroad markets to expand and continue their growth due to small size of Finnish market. As a result, many Finnish companies accumulate most of their revenue from other countries than Finland; for example, Kone yields only 3% of its 9-billion-euro revenue from Finland, which ranks only 9th out of the countries Kone operates in (Kone 2019; 35). In comparison, 25% and 15% of revenue come from China and United States, respectively.

1.2 Research gaps

M&As have been researched for decades. However, historically studies of M&A have been mainly focusing on financial aspects, with a top-down perspective from a buyer's point of view. In addition, M&A literate has been largely unable to identify key elements of successful M&As (Gomes, Angwin, Weber & Tarba 2013). Meglio and Risberg (2010) argue this is because researchers are using different measurements and approach angles in their research, which in turn leads to discrepancies in results.

Research show that there appears to be a disconnection between actions before and after the M&A (Gomes et al 2013). As M&As are often highly complex operations with different levels, layers and nuances to them, it is difficult to create a single working formula to precisely predict successfulness of a given M&A (Angwin 2007; Javidan, Pablo, Singh, Hitt & Jemison 2004).

Current M&A literature is mostly focused on analysing what executives should do to maximize effectiveness of M&As. Even so, executives often fail to achieve positive and desired outcomes (King, Dalton, Daily & Covin 2004). When being acquired, target companies are virtually always paid a premium, which boosts their stock prices considerably. As such, M&As are clearly creating short term value for shareholders of target company. However, situation for acquiring company is different. Even if long term profitability of acquiring companies is not great (King et al 2004), there appears to be a research gap regarding value creation on shorter term, especially in case of Finnish companies. Furthermore, M&A research widely sees shareholders as static actors, whereas active shareholders may seek to benefit from shocks to stock market, as it might result in transitory incorrect valuation levels (Perron, Chun, Vodonou 2013).

1.3 Purpose of the thesis and research question

The purpose of this thesis is to understand **if companies can create value through mergers and acquisitions**. For example, extensive research is done to identify common challenges related do mergers and acquisitions, which might cause minor issues or major problems for companies. As a result, this thesis offers valuable information for shareholders of companies engaging in M&A projects. Furthermore, effective means for successful execution of mergers and acquisitions are extensively discussed. This will give valuable information for companies and investors. This thesis will answer the following research question:

1) Can companies create value for their shareholders through M&As?

To support the primary research question, secondary research questions are:

2) What is the initial reaction of stock market following the M&A announcement?

3) How stock prices develop after initial reaction?

1.4 Delimitations

As there are considerable amount of companies engaging in M&As and divestments, certain practical delimitations must be made. As such, this thesis focuses solely on companies that fulfil the following three requirements: (1) the company has to be publicly traded in Helsinki stock exchange, (2) the company has to be big enough, thus belonging to OMX Helsinki 25 index, (3) financial information regarding M&As are published.

M&As can be carried out with various different payment methods, such as cash, equity or earn-out plan. While all these different methods have their own characterisations (Sankar & Leepsa 2018), they all have the same end result, which is M&A being implemented. As such, this thesis will handle all M&As equally, regardless of their payment methods.

1.5 Thesis structure

This thesis consists of five main chapters. The first chapter is Introduction, in which the topic is presented along with research question, gaps and delimitations. I will also describe how answer for research question will be achieved. Table 1 presents structure of the thesis.

The second chapter is a literature review of using M&As as strategical instruments. Subchapters are tightly linked to different functions and outcomes of M&As, varying from internal operations to reactions of stock markets. In addition, generalized categorization of M&A strategies are presented.

The third chapter is about data collection and research methodologies, and ultimately it explains why I have chosen a certain methodology approach in my thesis. I am also describing how the data is collected and handled. I will also expand on delimitations here and explain why certain companies are targeted in this thesis.

The fourth chapter focuses on empirical results and answering hypotheses that was presented in chapter two. An extensive analysis of data is made, and special emphasis is placed on differences in results between the companies.

The fifth and final main chapter is Discussion and conclusions, in which I will present a summary of my findings. Research questions are also answered. I will also present practical recommendations based on my results. I will also offer my suggestions for further research on this topic.

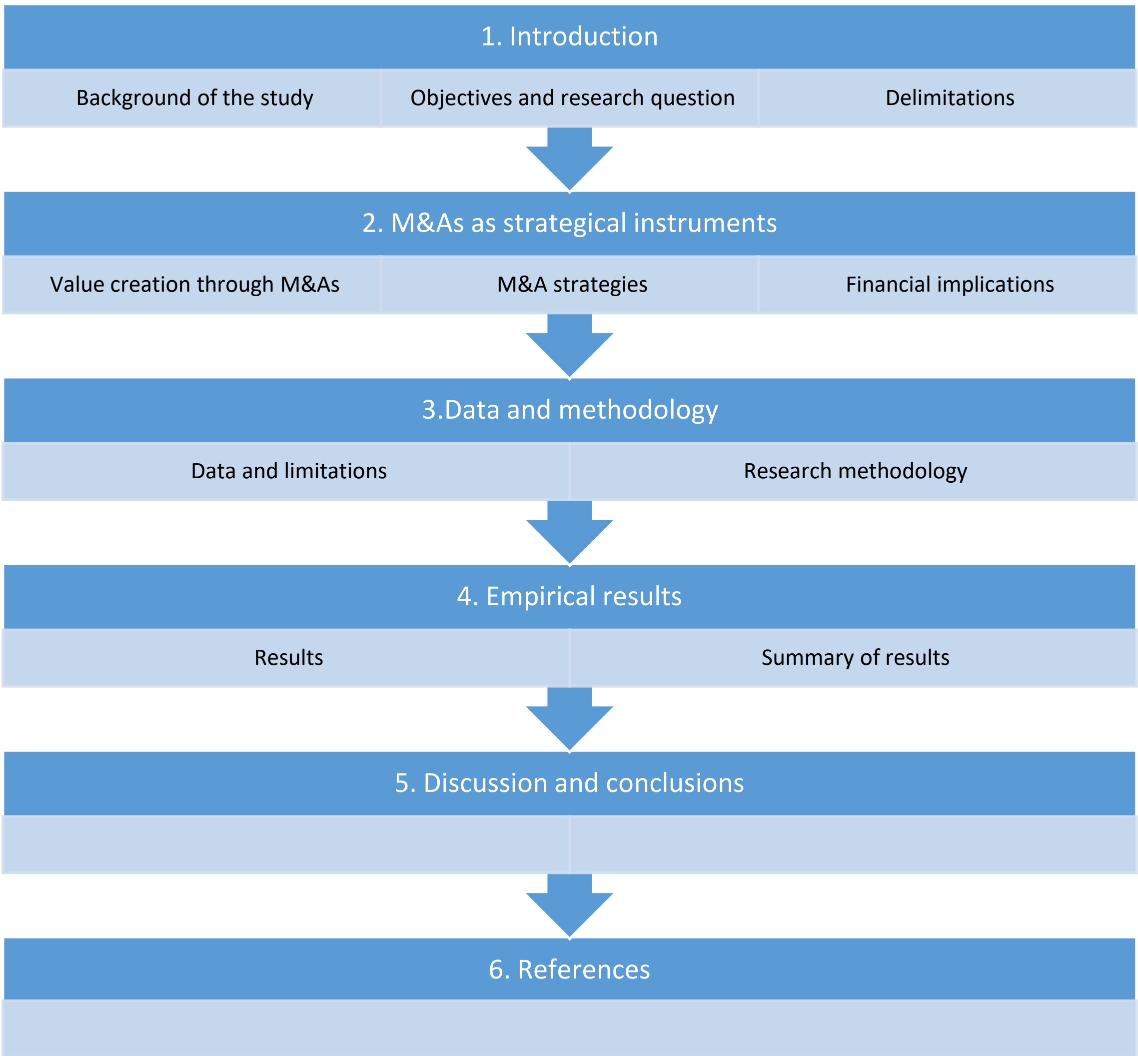

Table 1 – Thesis structure

2 M&As as strategical instruments

This chapter begins by explaining how M&A typically influence companies. Further, this chapter discusses how companies can create or destroy value by engaging in M&A and divestment operations. In addition, possible similarities between various successful and unsuccessful M&A operations are discussed.

According to Meglio and Risberg (2010), universal agreement over what makes M&As successful or not, does not exist. Meglio and Risberg (2010) are of the opinion that it is because researchers approach studying M&As with differing motives and objectives. In practise, this means that different researchers are measuring different performance factors with different research methods, which makes it illogical to compare such studies directly (Meglio & Risberg 2010; Zollo & Meier 2008). As such, M&A-related literature and research remains largely contradictory and fragmented (Gomes, Angwin, Weber & Tarba 2013). This thesis aims to identify if companies are able to overcome these challenges, and create value for their shareholders.

2.1 Creating value through M&As

Larsson and Finkelstein (1999) have noted that M&A synergy is best achieved when the level of similarity and complementarity between the acquirer and acquired are high. In practice, this means that the companies are a great strategic fit. To support this notion, Wang, Sorensen & Moini (2018) state that as M&A is a strategy that changes the available resources of the company, it is important that acquired resources are utilized effectively. As such, synergistic benefits are achieved by reconfiguration and integration of new and old resources. Efficiency can also raise through economies of scale, especially in stable industries (Häkkinen, Nummela & Taalas 2010). In addition, there is a positive correlation between post-M&A value creation and pre-M&A performance levels of the acquirer and acquired company. In essence, this means that profitable and well-functioning companies with strong resource bases are prime candidates for successful M&As, be it either as an acquiring or acquired company (Wang, Sorensen & Moini 2018).

Historically, M&A research have separated their focus either on pre-merger or post-merger factors. Gomes et al (2013) challenge this tradition, as they argue that both aspects should be combined together to achieve desired M&A outcomes. In practice, this means that high synergy potential, which has been recognized pre-deal, cannot be fully realized unless post-deal organizational fit is good between the companies. Research supports this notion, as it is proven that ability to connect pre- and post-merger phases correlate with better M&A results (Weber, Tarba & Rozen Bachar 2011). These results are achieved by utilizing known pre-merger factors such as strategic and organizational fit factors in choosing the correct post-merger approach.

Furthermore, it has been researched that strategic complementarity leads to less resistance among employees and managers. This helps in achieving synergy, thus raising M&A effectiveness and accelerating value creation process (Tarba, Ahammad, Junni, Stokes & Morag 2019). This is best achieved by seamless transition from pre-acquisition to post-acquisition process (Gomes, Angwin, Weber & Tarba 2013).

Even though M&A research vary from one another and there are various distinctions for M&A process steps, a key moment in all M&As is when the ownership is transferred to the acquiring company. This ownership transfer is essential for lawful reasons, and for the fact that post-acquisition integration cannot truly be executed unless the acquiring company has commanding ownership. As such, M&A literature generally works within this framework of dividing M&A process into pre-merger and post-merger activities. (Gomes et al 2013).

A major obstacle in value creation through M&As is failure to successfully move from pre-acquisition to post-acquisition phase. This integration phase is often hindered by asymmetrical information, which leads to uncertainty regarding e.g. requirements, quality control and implementation strategy (Gomes et al 2013; Angwin 2001). A comprehensive due diligence can be utilized to minimize this information asymmetry (Boyle & Winter 2010).

Companies must also consider their allocation of resources and time to different phases of the M&A; focusing too much on e.g. post-merger activities may hinder effective pre-merger due diligence process (Tarba et al 2020). A typical mistake is including HR too late in the M&A process, as their earlier participation could have given warnings about e.g. potential cultural clashes and difficulty in retention of key employees (Weber, Tarba & Oberg 2014).

Even though M&As are carried out to create more value to shareholders (Sudarsanam 2010), M&As are not always leading to improved financial performance (King, Dalton, Daily & Covin 2004). In fact, quite the opposite is the truth, as “M&A activity has a modest negative effect on the long-term financial performance of acquiring firms” (King et al., 2004). Even so, the amount and size of global M&As continues to increase even while their success rate remains modest at best (Welch, Pavicevic, Keil & Laamanen 2020; Gomes, Angwin, Weber & Tarba 2013). This is linked to the fact that no universal indicators or predictors for M&A successfulness have been found, which in practice hinders long-term predictability of M&As (Ahammad, Tarba, Liu & Glaister 2016; Stahl & Voigt 2008).

Kiriakov & Sidenko (2011) discuss the paradox regarding M&As, as approximately two thirds of them fail, but their popularity only continues to rise. It can be argued that it has become a natural way for companies to grow even when failure rates remain high. It is also important to note that majority of the biggest companies in the world have gone through several acquisitions and mergers. In addition, these large companies are often continuing their international M&As in order to maintain growth and remain competitive (Calcagno & Falconieri 2014). Martynova & Renneboog (2008) demonstrate that poor acquisitions are sometimes influenced by both herd behaviour and arrogance at executive level.

2.1.1 Importance of timing

M&A profitability is linked to the stage of which M&A wave is at. Research and data suggest that M&As carried out in late phase of the wave are, on average, less profitable that those carried in the beginning of the wave (Goel & Thakor 2010). As such, it is important to engage in M&A activities before they become too popular. Furthermore, according to Martynova & Renneboog (2008), these M&A waves are initiated by economic recovery followed by rapidly growing stock market. Ultimately, these M&A waves have always ended in a stock market collapse.

Preceding stock market collapses of 2001 and 2008, M&A activity in both value and quantity reached their historic peaks during the boom years of 1998-1999 and 2006-2007. M&A value decreased by 58% and 55% in 2001 and 2008 respectively, compared to the previous year (Erxleben & Schiereck 2015; Jovanovic & Rousseau 2008). Various research proves that even though acquisitions made during bull market are more profitable in short-term than those made in bear market, they are less profitable and yield lower long-term abnormal return than those made during bear market (Goel & Thakor 2010; Bouwman, Fuller & Nain (2009); Rhodes-Kropf & Viswanathan (2004). When combining these two factors, it is evident that there is a paradox where companies are engaging in M&A activities during times when it is not profitable for them or shareholders in the long run. This is at least partly caused by executives being driven by personal interest, such as generous bonuses being linked to stock price (Erxleben & Schiereck 2015).

During bull market, acquisition news is often received with enthusiasm boosting stock prices, thus creating income for executives (Erxleben & Schiereck 2015). Research (Shleifer & Visnhy 2003; Rhodes-Kropf & Viswanathan 2004) demonstrate that temporarily overvalued equity can be used to acquire a suitable target company when paying it with own, currently overvalued, equity instead of cash. In essence, executives of these temporarily overvalued companies can utilize transitory ineffectiveness of stock market valuations to their benefit.

On the other hand, bear market offers exiting possibilities for acquiring companies, as valuation levels are down. Troubled companies are more likely to sell valuable departments or divisions to raise capital to survive challenging times. This phenomenon is presented in Figure 1. In addition, as there is less euphoria during bear market, it appears that companies are making wiser and more suitable investment decisions. Data suggests that small target companies are more profitable than big ones during bear market due to working on smaller financial margins and without considerable back-up funds which could carry them over hard economic times. Even though news and market reaction to acquisitions are often mixed at best due to prevalent financial uncertainty, acquisitions during bear market, on average, are creating more value for shareholders. (Erxleben & Schiereck 2015; Bouwman et al 2009; Martynova & Renneborg 2008)

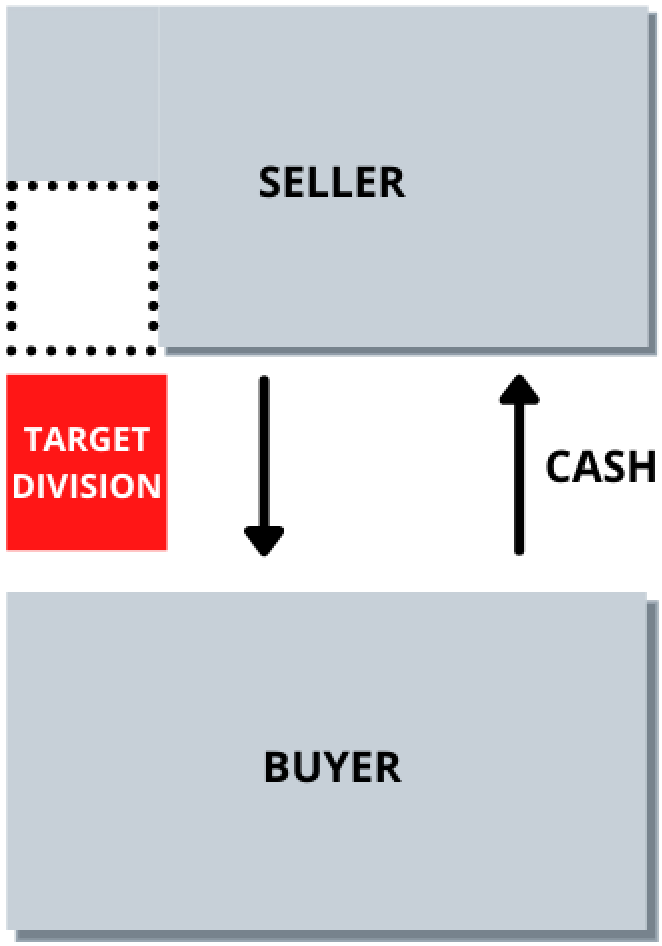

Figure 1. Acquisition of a division. Source: ***Own construction***

2.1.2 Pre-M&A activities

M&A process begins with recognizing a need for strategic partner. The first step requires thorough due diligence to find a suitable partner, which has e.g. matching strengths, suitable organization structure and low barriers for integration. These factors combined with "resource similarity and complementarity, combined relational capabilities and partner-specific knowledge" (Wang & Zajac 2007) are proven to correlate with successful outcome of M&As. (Angwin 2001; Gomes et al 2013)

Paying the right price is important in achieving the desired return. Numerous financial research about M&As are revealing that paying too much is a big reason for failure. This is especially important in cross-border mergers, as cultural and legal differences are enlarging information asymmetry between the target and acquirer. Cultural differences are also influencing how high premiums are in M&A transactions; European companies are paying more than 3 times higher premiums than their American counter parts, which in turn makes it tougher for European companies to achieve their goals for the acquisition. (Gomes et al 2013; Seth, Song & Pettit (2000), Inkpen, Sundaram, Rockwood 2000)

According to Gomes et al (2013), similarity in size between the companies is of utmost importance in M&A process. Large companies acquiring relatively tiny companies easily leads to suboptimal outcomes as the acquirer does not pay enough post-deal attention (Moeller, Schlingmann & Stulz 2004; Gomes et al 2013). In fact, empirical data collected by Finkelstein & Haleblian (2002) suggests that resemblance in company size correlates with positive outcome.

Previous experience in M&A activities tends to correlate with successfulness of M&As (Gomes et al 2013). As such, those that have amassed this valuable experience through e.g. continuous learning (Vermeulen & Barkema 2001) are in a prime position to perform successful M&A operations. On the other hand, previous experience is only useful if the past M&A processes have been executed properly with required attention to e.g. merger process management (Zollo & Singh 2004). As a result, companies without prior experience and knowledge of M&As can utilize external consultants to maximize their M&A performance (Delong & Deyoung 2007).

During courtship period, the two companies can familiarize themselves with one and other. This period is helpful in determining if the companies are a good match for a merger. (Gomes et al 2013.) Usual examples are e.g. engaging in a joint venture, operating as trade partners and having interlocking directorate (Stuart & Yim 2010). These actions can be of substantial value in negotiations through increased trust and chemistry of the companies, especially in cases where cultural differences are large (Gomes et al 2013; Barkema, Bell & Pennings 1996).

Communication before, during and after the acquisition plays an integral role in determining the eventual outcome of the acquisition process. Subpar communication has been proven to undermine M&A successfulness (Light 2001; Angwin 2001), as essential stakeholders may become anxious, thus impacting their contribution negatively (Gomes et al 2013). According to Teerikangas (2012), employee reactions are highly linked to communication and actions of the acquirer; open and honest communication regarding future plans and goals plays a key role in keeping employees motivated towards their work while also controlling resistance for change.

Companies must also consider their future compensation policies before engaging in M&A operations. There is a danger that compensation packages and incentives can create a conflict between individual gains and corporate ambitions (Inkpen, Sundaram & Rockwood 2000). To combat this, acquiring companies have the possibility to motivate executives of the acquired company with e.g. earn-outs, in order to guarantee that the acquired company continues to operate as effectively as possible (Anslinger, Copeland & Thomas 1996). However, newer research has shown that these type of equity-based compensation schemes may be used by opportunistic managers to enlarge their own personal bonuses (Grinstein & Hribar 2004; Devers, Cannella, Reilly & Yoder 2007).

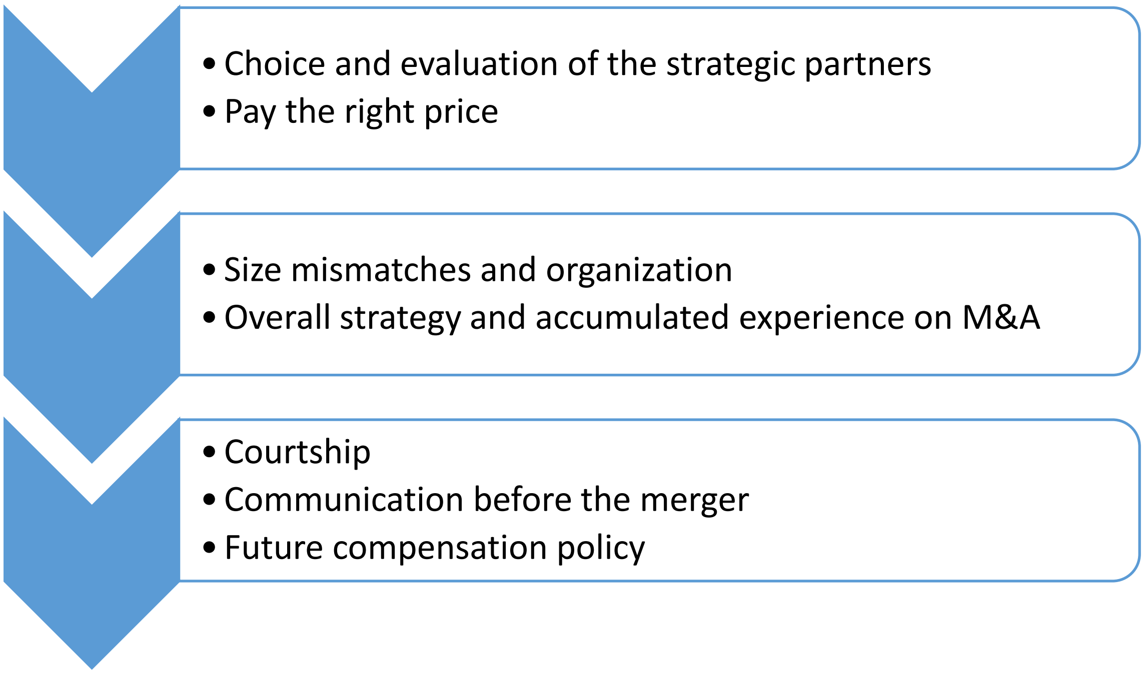

Table 2 – Pre-merger phases (Gomes et al 2013)

2.1.3 Post-M&A activities

Acquired companies, which become clear subsidiaries, tend to perform better when they are given at least a certain degree of autonomy. Their superior local knowledge combined with new resources presented by the acquirer can be utilized in creating innovating solutions for local customers. On the other hand, integral human capital can be quickly lost if too much emphasis is placed on short-term efficiency, which in practice means e.g. dismissals and general downsizing. (Meyer & Lieb-Dóczy 2003.) The underlying challenge regarding integration is that in order to achieve desired synergies, the acquired company might lose its key value creation ingredients due to substantial changes in e.g. employees and organizational routines (Gomes et al 2013). As such, the rate of integration can be seen as a balancing act, where it is very hard to cherry pick only the positives.

Clarity of communication between managements of acquirer and target company correlate with successfulness of M&As (Gomes et al 2013). In addition, having clear plans and future directions help in succeeding in post-M&A operations (Vasilaki 2011). This can be achieved by appointing a top executive who is in charge of leadership in the target company. If he/she comes from the acquiring company (“Insider”), the role is reminiscent of a supervisor, whereas an appointment from the outside (“Outsider”) is often used when sizable changes are made to the target company (Gomes et al 2013; Angwin & Meadows 2009). Regardless of the choice between Insider or Outsider, the key role of management is to recognize the most important units and enhance their cooperation through new interrelationships while eliminating redundant units (Angwin & Meados 2009; Gomes et al 2013). Vasilaki (2011) describes that no universal guidebook should be used, but instead understand that each case is unique from one another.

Even though moving quickly during the implementation phase can cause problems through employee discomfort, uncertainty and customers being forgotten (Angwin 2004; Gomes et al 2013), the cost for losing momentum and acting too slow is even greater (Light 2001). On opposite, however, Ranft & Lord (2002) claim that in case companies which had slower integration speed, trust level between employees were higher. Furthermore, studies by Homburg & Bucerius (2005) and Angwin (2004) state that it is impossible to determine a perfect speed, as moving fast or slow have their own unique benefits and weaknesses. Nonetheless, speed in early parts of the integration allows companies to achieve so called “early victories” which can be used to inspire all stakeholders, from employees to investors (Gomes et al 2013).

As post- M&A period requires considerable amount of attention to integration, managers might fail to pay attention to day-to-day activities (Angwin 2001). As such, important aspects such as innovation and internal growth might be neglected (Vermeulen & Barkema 2001). In fact, internal growth and development are preferred over acquisitions in some companies due to risk aversion (Ghemawat & Ghandar 2000; Gomes et al 2013). In the cases where merger or acquisition is the chosen path, research proves that creating a coordination unit correlates with a positive outcome of the process. This coordination unit should be introduced even before the M&A contract has been signed. (Inkpen et al 2000; Gomes et al 2013)

As mentioned earlier, uncertainty of employees after the M&A should be treated as quickly as possible. As such, communication is a key factor in ensuring a beneficial outcome of the process (Gomes et al 2013). More precisely, introducing good human resource practices such as effective communication enhances the implementation process (Weber, Rachman-Moore & Tarba 2012). Importantly, managers should be making only promises that they are able to keep (Light 2001). As such, managers should avoid overcommunication. Instead, managers can benefit from sending ambiguous and slightly vague messages to maintain certain amount of flexibility in their own operations (Weber et al 2012). Furthermore, differences in national cultures must be considered, as they dictate the necessary amount of communication (Weber & Tarba 2011).

Table 3 – Post-merger phases (Gomes et al 2013)

2.2 Motives for M&A

Understanding why M&A is carried out gives a better understanding of the whole M&A process, as motives influence what type of companies are targeted, how they are valued and how their successfulness is measured (Hassan, Ghauri & Mayrhofer 2018; Porrini 2004). Researchers have found out three distinct categories for M&A motives, which are (1) improved economic performance, (2) personal benefits for managers and (3) increased market power (Hassan, Ghauri & Mayrhofer 2018; Brockman, Rui & Zou 2013; Boateng, Qian & Tianle 2008). M&As driven by self-interest of managers tend to yield subpar outcome (Hayward & Hambrick 1997), while ineffective due diligence in relation to M&A motives, target setting, and integration processes is also preventing to maximize potential outcome (Haspeslagh & Jemison 1991). As such, it is wise to list motives and goals rationally before the process and utilize them when assessing the outcome (Epstein 2005).

Renneboog & Zhao (2014) prove that information advantage gained by directors affect profitability of M&A. Executives can gain direct and indirect knowledge through their roles as e.g. board members in other companies. This information can be utilized in making smart acquisitions, which are sometimes rewarded by higher abnormal announcement returns in comparison to those done without obvious information advantage. Explanation for this is the belief that bidder CEO is more likely to know something that can create value for the acquirer. However, M&As carried out when utilizing said connections have sometimes failed when the two parties are clear friends, due to e.g. overvaluation of the target company (Ishii & Xuan 2014). As such, close connections between directors in M&As can be beneficial, but there are clear downfalls that must be avoided.

2.3 M&A strategies

Even though M&As have been thoroughly studied, it is hard to give exact generic distinctions, as M&As can widely differ from one and another and require context-specific approach and analysis. Even so, Brueller, Carmeli & Markman (2018) have created a model containing of different M&A strategies, post-merger integration (PMI) outcomes and Human Resource Management (HRM) practices.

Merger and Acquisition–Postmerger Integration–Human Resource Management Relationships: Construct Labels, Functions, Definitions, and Examples

Merger and Acquisition Strategies	**Annex & Assimilate**	**Harvest & Protect**	**Link & Promote**
Merger and acquisition goals	Absorbing assets (primarily tangible) from targets	Capturing and preserving intangible assets (e.g., capabilities, partnerships) from targets	Linking self-interest to shared interest by cocreating boundary-spanning opportunities for both firms as they operate independently
Strategic and operational leadership held by . . .	Acquirer	Target holds some strategic and operational power, but acquirer sets the tone	Both targets and acquirers hold ample strategic power and operational leadership
PMI Outcomes	**Absorption**	**Preservation**	**Symbiosis**
Examples	The merger of United–Continental Airlines	Cisco's acquisition of IronPort and Linksys	EMC's acquisition of VMware
Autonomy of acquired target	None (target is dissolved)	Moderate and usually operational and tactical	High and strategic
Relationship power	Asymmetrical: All power held by acquirer	Moderate: Most power held by acquirer	Symmetrical and synergistic
Interfirm trust	Minimal	Moderate	High
Human Resource Management Practices	**Ability**	**Ability & Motivation**	**Ability, Motivation, & Opportunity**
Examples	Recruitment, selection, training	As in left cell, plus: Performance and development programs, competitive pay systems, upward career mobility	As in left cells, plus: Flexible job designs, cross-firm engagement programs, transparent management
Practices designed to . . .	Enhance personnel skills and abilities of personnel	As in left cell, plus: Enhance motivation of personnel	As in left cells, plus: Empower employee to engage at higher levels across both firms
Human capital focus	Removal of redundancies and integration of human capital	As in left cell, plus: Personnel retention and capability alignment	As in left cells, plus: Reciprocal empowerment and cause-based programs that transcend firm boundaries

Table 4 – Brueller, Carmeli & Markman (2018)

The researchers have categorized M&A strategies into three groups; *annex & assimilate*, *harvest & protect* and *link & promote*.

Annex & assimilate strategy is used to acquire key assets of the target company, such as personnel, resources, or other mostly tangible assets. In addition, unprofitable units are cancelled, and unneeded personnel are made redundant (Brueller, Carmeli & Drori 2014). This strategy works well for large global companies targeting small local companies (Horovitz 2004), where they can assimilate and integrate these small targets quickly and cost efficiently. When both the buyer and the target are large companies, annex & assimilate becomes substantially more complex and resource consuming project with a longer time frame, where benefits of synergy may be hard to be achieved (Chakravarthy & Lorange 2007; Brueller, Carmeli & Markman 2018).

Harvest & protect strategy allows buyer to capture intangible assets such as know-how and partnerships, which can then be used to e.g. improve R&D and product offering while also entering new markets (Puranam, Singh & Chaudhuri 2009). These acquisitions also allow companies to relocate their personnel to more productive tasks to enhance operations even further. Typical small targets are start-ups with strong technical knowledge, but who are lacking e.g. managerial know-how and capital (King, Slotegraaf & Kesner 2008). Larger firms are interested in these small start-ups, as the knowledge and innovations they possess would be expensive and time-consuming to create internally (Puranam, Singh, Chaudhuri 2009). One key distinction for harvest & protect is how it aims to create value – little to no emphasis is placed on scale advantages. Instead, value is created by preserving acquired know-how and trying to expand it to whole company (Brueller, Carmeli & Markman 2018).

Link & promote strategy aims to let acquired company to operate as independently as possible, while stimulating boundary-spanning and interfirm operations with an aim to make both companies prosper (Chakravarthy & Lorange 2007). Interfirm learning is used extensively to boost e.g. cross-boundary agility, innovation and knowledge exchange (Brueller, Carmeli & Markman 2018). This is a demanding M&A strategy, as both companies are expected to remain autonomous, self-sufficient, and strategically independent (Brueller, Carmeli & Markan 2018), but if done correctly, it can result in clear synergistic benefits and value creation for both parties (King, Slotegraaf & Kesner 2008).

Even though companies often also seek short-term benefits from M&As, their main goal especially in case of international M&As is to secure long-term survival of the company by growing operations volume (Anwar 2019).

2.3.1 Friendly takeovers

Friendly takeovers represent a scenario where management and board of directors agree with being acquired, thus recommending current shareholders to accept incoming takeover bid. In most cases, friendly takeovers retain at least some of previous managers after M&A operation has been carried out. As such, executives may have a personal incentive to lean towards friendly takeovers over hostile takeovers (Loyola & Portilla 2016).

2.3.2 Hostile takeovers

Hostile takeovers are more popular when there is an external sentiment that the current management is mismanaging its resources, and that profitability of the company could be increased with a new, allegedly more talented board of directors (Zhou & Guillén 2019). As such, hostile takeovers can be seen as a way to motivate and put certain level of pressure on managers to perform their duties well (Morck, Shleifer & Vishny 1989). Morck et al (1989) further argue that hostile takeovers maximise value creation for shareholders, as the share price tends to soar after takeover plans are announced. Furthermore, Shleifer & Vishny (2003) note that in hostile takeovers usual payment method is cash, rather than stock.

2.4 Divestments

Majority of companies favour buying to selling when restructuring their operations, which in practice means relying on M&As instead of selling inefficient units (Whale 2015; Dranikoff, Koller & Schneider 2002). This sometimes comes at a cost, as operating on numerous unrelated segments can cause stock price being traded at 5-15% lower when comparing it to sum of the company's parts. This phenomenon is called a conglomerate discount. (Berger & Ofek 1995; EY 2019)

Companies are most likely to divest due to unit's subpar performance in relation to competition, streamlining operations or because of receiving a lucrative offer they could not pass (EY 2019). Recent increase in shareholder activism has led to de-conglomeration, which in turn has made companies more aware and active in their portfolio management (EY 2019; Whale 2015). Statistics support this evolution, as in 2019 84% of global companies are expecting to engage in divestments in the next two years, compared to lowly 20% in 2015 (EY 2019).

Various researchers have claimed that a phenomenon of conglomerate discount can be overcome, and value creation is possible with divestments (Erxleben 2015; Dasilas & Laventis 2018) even though majority of empirical studies are focused on M&As (Brauer 2006). Finnish insurance company Sampo has seen its valuation steadily grow ever since the announcement of selling its ownership of Nordea Bank, thus focusing solely on insurance segment. Risks are lower and higher valuations are generally accepted in insurance segment compared to banking segment. Furthermore, capital raised through selling of Nordea will be distributed to shareholders as dividends or buybacks, while also having enough capital for new, suitable acquisitions. (Inderes 2021a; Inderes 2021b)

2.5 Financial outcomes of M&As

M&A intentions are often kept secret or explained vaguely until the official deal announcement is made public. This is generally done to keep the M&A process running smoothly while retaining flexibility of the company. In addition, vague M&A intentions are used to avoid leaking key information to competitors. Financially speaking, it has been studied that M&As carried out without comprehensive public explanations are more profitable in the long run; companies not sharing detailed public M&A information experience nearly 10 % better long-term stock performance than their counterparts. (Guo, Li, Hu & Wang 2019)

2.5.1 Market reaction to M&A news

While the true outcome of M&A is impossible to predict when the deal is announced, stock market reactions are the first platform where to examine the possibility of different outcomes. Initial reaction consists of three categories. Firstly, the announcement gives new information about the value and size of both buyer and target companies. Secondly, stock prices react to M&A announcement based on estimated synergies between the companies. Thirdly, stock market is reacting to how these gains in synergy are going to be split between buyer and target company. In essence, the more M&A is estimated to benefit a company, the more its share price is going to rise. In some cases, both companies see their share price rise, in some just the other, and sometimes both might drop if the deal is deemed bad for them both. (Barraclough, Robinson, Smith & Whaley 2013)

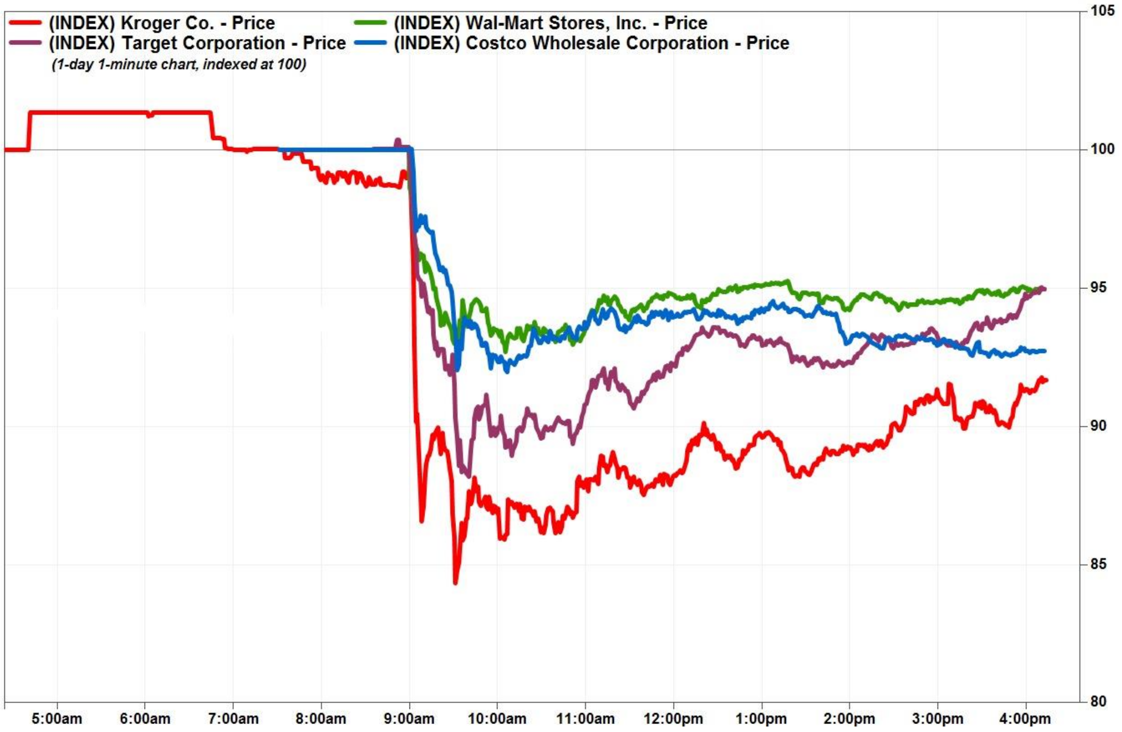

Figure 2 – Stock price reactions to Amazon – Whole Foods acquisition (Nadar 2018)

M&A announcements also have indirect consequences. For example, when Amazon acquired grocery store chain Whole Foods in 2017, its competitors suffered a severe drop in share prices; after the acquisition was announced Walmart and Target were down 5%, while Costco and Kroger dropped 7% and 8% respectively. This situation is demonstrated in Figure 2. As such, it is evident that the market had high expectations for Amazon's acquisition of Whole Foods, practically at the cost of its rivals. (Nadar 2018)

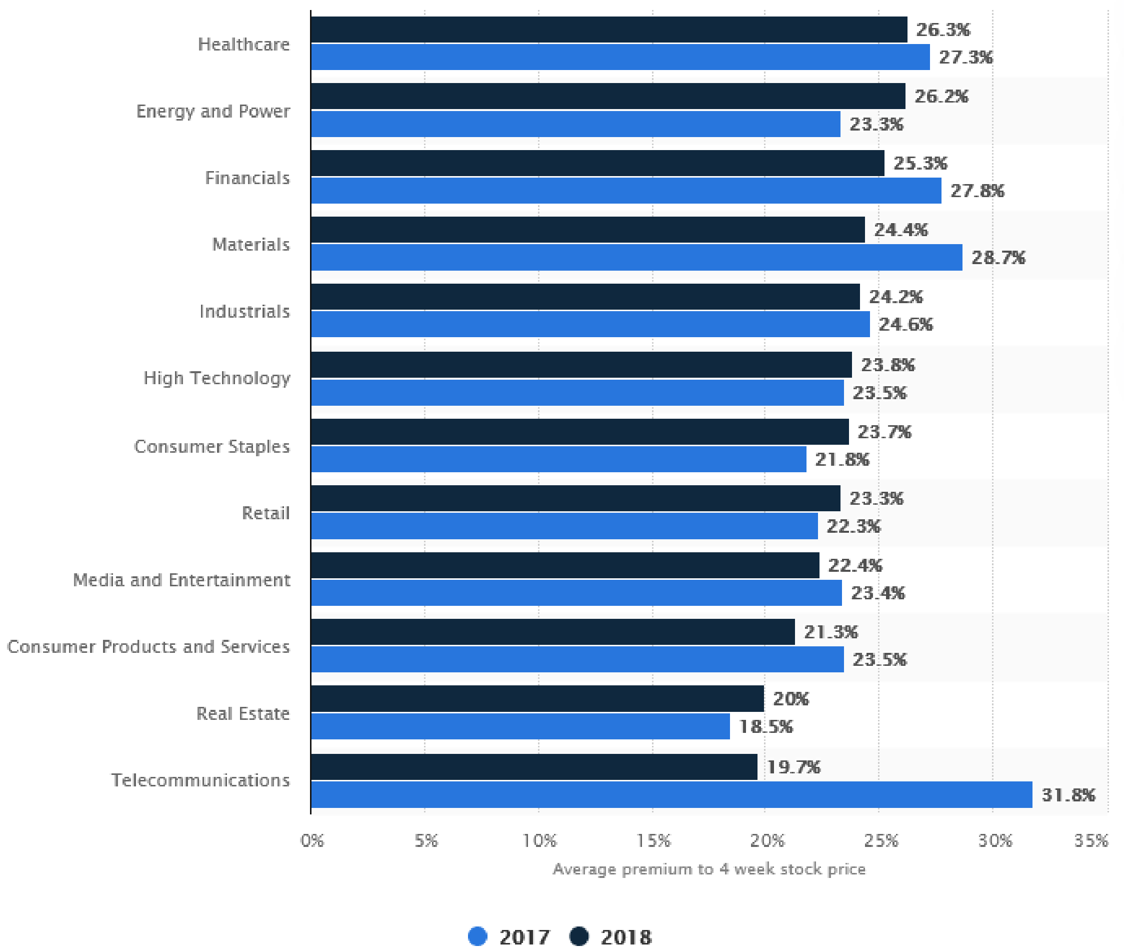

Figure 3 – Average premium paid in M&As (Statista 2018)

In M&As, it is typical that a premium is paid on top of the share price to tempt shareholders to sell their shares. For example, in the aforementioned Amazon – Whole Foods acquisition, this premium was 27% (Bloomberg 2017). This is in line with average premiums worldwide, as in nearly every industry the average settles between 20% and

30% (Statista 2018). In Figure 3, exact figures between different industries are presented. These premiums are instantly reflected in share prices, which naturally soar following M&A announcement. As such, short-term winners in most cases are shareholders of target company (Martynova & Renneboog 2008). In short-term, it is also important to note that when volatility rises, so does the possibility of ineffective, transitory valuation while stock price is finding its new balance area. This partly because of amplified interest towards acquiring and target company. (Geppert & Kamerschen 2008)

For acquiring companies, however, returns on average are close to zero. This is part of the reason why majority of M&As are seen as failures (Kiriakov & Sidenko 2011), and companies engaging in M&As as acquirers should not be expecting their stock prices to soar. Even though on average M&As seem lukewarm investments, there are wide variations between returns. Some companies are managing to create clear and significant value for their shareholders on both short- and long-term time windows. (Bruner 2002; Bruner 2004)

In a big meta-analysis study consisting of 55 399 M&A transactions carried out between 1950 and 2010, it was uncovered that only 47,6% of these transactions were creating value for the acquirers. This meta-analysis carried out by Meckl & Röhrle (2016) combined results from 32 studies, most of which had measured performance over a three-day window following the M&A announcement. Results of this meta-analysis suggest that companies should place great emphasis on risk analysis and evaluation of target companies.

2.6 Measuring M&A performance

When discussing outcome of M&As, it is important to distinguish stock performance and operating performance from one another, as there is no guarantee of positive correlation between the two. Stock price might be (inaccurately) influenced by e.g. prevalent market sentiment, while changes in accounting standards might skew earnings-based measures. Both pre-deal and post-deal time periods are vulnerable for earnings manipulations, as sellers intend to boost attractiveness of the company, while new executives can manipulate figures to present better performance than their predecessors (Rennebog & Vanstenkiste 2019; Healy et al 1992).

A major challenge in analysing M&A performance is impossibility of isolating the takeover effect from other influencing factors, especially when doing long-term analysis (Renneboog & Vansteenkiste 2019). When comparing short-term and long-term analysis of M&As, the latter is more fruitful, as all possible synergies are revealed, and market inefficiency is removed from the equation (Renneboog & Vanstenkiste 2019; Mitchell et. al. 2004). Even so, when analysing long-term performance of M&As, it is important to note that based on the chosen model, expected returns can quickly swing even by dozens of percentage points (Andrade et. al. 2001). In addition, accuracy and reliability of long-term expected returns analysis is highly sensitive to even minor errors, for example in risk analysis (Kothari & Warner 2007).

In typical cases, both short-term and long-term are measured by utilising an event study methodology. Event studies can further be divided into two categories – (i) comparing returns of event firms to set control firms that have been chosen due to suitability in e.g. industry and size. The other category (ii) utilizes regression analysis to determine alpha coefficient through e.g. capital asset pricing model (CAPM). One of the most popular approaches is calculating cumulative abnormal returns (CARs). In this model, a long time period is chosen which can begin before or after the acquisition, and all abnormal returns of this time frame are summed together. As most investors often hold assets over a longer period of time instead of hunting abnormal returns on a day-to-day basis, buy-and-hold abnormal returns (BHARs) method gives slightly different results, as it takes compounding effect into consideration, unlike CARs. As mentioned earlier, both CARs & BHARs are event study methodologies, which in practice means marking event date as t_0. This marks the date when M&A operation is announced. (Renneboog & Vanstenkiste 2019). Recently, Bessembinder et al (2018) have introduced a new method utilizing predicted benchmark results of both event and non-event firms to measure if realized returns for event companies following t_0 are abnormal.

In certain cases, companies seem to create value for their shareholders by losing M&A bids. According to Malmendier et al (2018), in close bidding contests between similar bidders based on their stock price evolution, profitability and other accounting measures, the losing bidder outperforms the winner by 24% over the next 3 years after the merger. Even though this research is strictly limited to merger contests and cannot be generalized to all cases, it proves that positive short-term abnormal returns do not guarantee long-term success.

Post-merger performance can also be measured by total factor productivity (TFP). Skilled acquirers enhance output of plants that they keep and sell those that are not as profitable. In most cases, the productivity of acquirer's own plants increases as well, perhaps linked to unlocked synergies. This research by Maksimovic et al (2011) discovers that clear majority of divestments following M&A are carried out in the first three years following the event. This is consistent with previously discussed findings of Gomes et al (2013) that speed is key in M&As.

2.7 Summary of theory and hypotheses

As has been discussed in this chapter, results of M&As vary from case to case, and research regarding the subject remains contradictory. This is partly due to researchers measuring different key performance indicators with different research methods (Meglio & Risberg 2010; Zollo & Meier 2008). As a result, M&A research remains contradictory (Gomes et al 2013).

Research shows that value can be created through M&As. This is the case especially when acquirer and target companies are complimenting each other well, and synergies are easier to achieve. Such companies create a great strategic fit, and they can allocate their new, mutual resources in a better way, thus creating value (Larson & Finkelstein

1999; Wang, Sorensen & Moini 2018). In addition, according to Häkkinen, Nummela & Taalas (2010), companies can benefit from M&As through increased economies of scale. To summarize, it is evident that there is a solid level of consensus among researchers that companies whose strengths fit each other naturally are prime candidates for being successful in their M&A operations.

M&As are carried out for variety of reasons, but three distinct categories have been found by researchers. Firstly, companies seek improved economic performance. Secondly, companies may seek increased market power. Thirdly, executives and managers are driven by their own personal, often monetary reasons to engage in M&As. (Hassan, Ghauri & Mayrhofer 2018; Brockman, Rui & Zou 2013). Unsurprisingly, M&As carried out due to self-interest of executives yield subpar financial return (Hayward & Hambrick 1997). As such, companies should engage in M&As only if it is for the right reasons – creating value for shareholders, not executives.

Even though executives can destroy value, they are also capable of creating it. Renneboog & Zhao (2014) uncovered that those executives who are e.g. board members in other companies can gain information advantage regarding M&As, perhaps by learning from mistakes, thus simply having more experience in M&A processes. However, if executives have too close connections, there is a danger of overvaluation of the target company (Ishii & Xuan 2014). As such, executives are recommended to be careful when engaging in M&As where both parties know each other, perhaps even too well.

Even though clear and transparent communication to investors is seen as a beneficial virtue, it may sometimes be detrimental for value creation. Companies choosing a more vague and secretive approach to M&A announcements were proven to be more profitable investments for their shareholders; they outperformed their open and transparent counterparts by nearly 10% in long term comparison. According to research, this may be linked to secretive companies retaining their freedom, flexibility and ability to change strategies without much trouble should it be necessary. (Guo, Li, Hu & Wang 2019)

There is a paradox where M&As are continuously more and more popular, but their successfulness does not rise (Kiriakov & Sidenko 2011). In fact, companies who are acquiring another company, should be prepared to be disappointed, as returns are modest, if not non-existent (Bruner 2004).

While the true outcome of M&A is impossible to predict when the deal is announced, stock market reactions are the first platform where to examine the possibility of different outcomes. Initial reaction consists of three categories. Firstly, the announcement gives new information about the value and size of both buyer and target companies. Secondly, stock prices react to M&A announcement based on estimated synergies between the companies. Thirdly, stock market is reacting to how these gains in synergy are going to be split between buyer and target company. In essence, the more M&A is estimated to benefit a company, the more its share price is going to rise. In some cases, both companies see their share price rise, in some just the other, and sometimes both might drop if the deal is deemed bad for them both. (Barraclough, Robinson, Smith & Whaley 2013)

For acquiring companies, however, returns on average are close to zero. This is part of the reason why majority of M&As are seen as failures (Kiriakov & Sidenko 2011), and companies engaging in M&As as acquirers should not be expecting their stock prices to soar. Even though on average M&As seem lukewarm investments, there are wide variations between returns. Some companies are managing to create clear and significant value for their shareholders on both short- and long-term time windows. (Bruner 2002; Bruner 2004)

Meckl & Röhlre (2016) combined a meta-analysis, which showed that even on a short-term, M&As are in most cases destroying value instead of creating it. When combining this with a strong consensus of M&As not being profitable on a longer time frame either (Erxleben & Schiereck 2015; Goel & Thakor 2010; Kiriakov & Sidenko 2011), the question remains if and how shareholders can influence value creation chain with their own actions? Research has shown that some executives have wisely benefitted from transitory ineffectiveness of stock market valuation to their benefit, e.g. utilizing equity payment method when buying on bull market, and acquiring overly cheap targets in a bear market for cut-out price (Shleifer & Vishny 2003; Rhodes-Kropf & Viswanathan 2004). In addition, Geppert & Kamerschen (2008) note that following M&A announcement, volatility of companies in question is rising. As a result, chance of stocks being wrongly valued rises. This opens a possibility for active shareholders to create value for themselves.

When summarizing the theoretical part of this thesis, it is evident that M&As are not certain to be profitable for companies who are acquirers. Target companies are enjoying soaring stock prices in short-term, but this is not necessarily the case for acquirers. However, increase in volatility following M&A announcement also increases possibility of stock market imperfections regarding valuation levels. Following Geppert & Kamerschen (2008) and Shleifer & Vishny (2003) and their research regarding increase of volatility and possibility of market misvaluations, the first hypothesis is:

H_1: Stock prices are likely to swing considerably right after M&A announcement has been made.

However, after the dust begins to settle and stock market has had time to digest consequences of M&A announcement, M&A research is quite unanimous in that mergers or acquisitions do not create value for shareholders of acquiring company, neither on short- (Meckl & Röhlre 2016) nor long-term time frame (King et al., 2004). As this thesis focuses on analysing short-term performance of companies compared to OMX Helsinki 25 index, we can form our second hypothesis:

H_2: Companies engaging in M&As as acquirers are likely to underperform compared to OMX Helsinki 25 over the chosen time period of one month.

3 Data and methodology

In this chapter, different data collection and methodologies are presented. Choices made regarding methodological approach and data collection are explained. Limitations related to data are also presented and explained.

3.1 Data and limitations

To start the empirical part of this thesis, data was collected. Years were limited to 2012 – 2022, in order to get relevant and fresh data. Only those acquisitions where the case company was acquirer, were considered. In mergers, there were no limitations. Divestments were disregarded. In addition, the company had to be publicly traded in Helsinki stock exchange as it is challenging to obtain required financial information from private companies. Furthermore, price paid for the acquisition had to be announced in order to examine its effect on stock price reactions. Lastly, companies had to be part of OMX Helsinki 25 at the time of M&A announcement. Only the biggest M&As were considered; 7 of deals examined in thesis belong to the list of 10 biggest M&A deals of Finnish stock exchange history. The missing 3 were discarded for being either spin-offs, or target and acquirer being part of the same conglomerate. Both reasons may create discrepancies in deal valuation, thus being omitted from this data set.

As mentioned, all chosen companies are part of OMX Helsinki 25, which means that they are some of the largest companies in Finland by their market capitalization. Some of the companies of HEX25, e.g. Kone and Neste, have been active in utilizing M&As, but they have a consistent policy of not announcing acquisition prices. This means that in this thesis, it is impossible to analyse profitability of these types of M&As when taking into consideration chosen time frame. While it is impossible to give a precise answer why companies such as Neste and Kone do not wish to disclose announcement prices, one clear similarity between them is concentrated ownership. Neste is 44,22% owned by Finnish Government (Neste 2022), while 62,29% of Kone's votes are controlled by majority shareholder Antti Herlin (Kone 2022). In addition, other Herlin family members also own considerable stake in the company. As such, these companies may feel that they do not have to be as transparent as companies that have more diluted ownership. This may offer them strategical advantage, as their competitors cannot learn all details of M&As.

All data was collected utilizing Bloomberg Terminal at University of Vaasa. Additional data has also been collected from stock exchange releases and companies' own home pages, and has been referred to accordingly.

3.2 Research methodology

There are various theories related to research approach, and they all have their own characterisations. Different choices are discussed in the following subchapter, and explanation for chosen approach is given.

As for the methodological choices, the data can be collected in two different ways. Quantitative research uses number-based data, which is often presented in e.g. charts and statistics, which makes it easier to interpret gathered data in a meaningful way. On the other hand, qualitative research is based on words rather than numbers. When qualitative approach being used, researchers can aim to get a deeper understanding behind the numbers by e.g. conducting interviews. If both quantitative and qualitative methods are used, chosen approach is called mixed methods research. (Saunders et al 2016)

Theories are traditionally examined in three different ways, which are deductive, inductive or a combination of both, abductive. Deductive approach is mostly used with quantitative approach, whereas inductive can be used with both quantitative and qualitative approaches. (Saunders et al 2016)

Event study method is widely used in academic studies of finance, especially when researching M&As (Tuch & O'Sullivan (2007). it can be used to measure how certain event influences chosen variable (Benninga 2008). Event study method is based on setting a clear timeline for duration of the study (MacKinlay 1997).

This thesis will use quantitative method while utilising a timeframe setting based on event study method. This decision is made, as quantitative method is highly suitable when collecting vast amount of precise numerical data like in this thesis. This helps discovering if, and when, active shareholders can benefit from their companies engaging in M&A. Setting a clear time frame helps to measure only short-term returns. Furthermore, this thesis is done by utilising a deductive approach, as existing theory will be tested with fitting hypotheses and research.

OMX Helsinki 25 (HEX25) is the leading share index of Helsinki stock exchange. HEX25 consists of the 25 most traded stocks on the Helsinki stock exchange. The maximum weight of one company is limited to 10 percent. Possible changes to companies in HEX25 are revised twice a year. As the companies in HEX25 have the highest liquidity of Finnish companies, it is the best suited index to analyse stock price reactions. In addition, as companies within this index are simultaneously the biggest companies of Helsinki stock exchange, they are prime candidates to engage in large, possibly international M&A operations. (Nasdaq 2022)

To minimize the influence of global financial fluctuations, all stock prices are compared to OMX Helsinki 25 (HEX25) index in the same time period. Reference points are *t*+1, *t*+5 and *t*+*month*, where *t* represents the previous trading day of announcement date. This is done so it does not matter if the announcement is given in the evening just after the trading has closed, or in the morning just before it opens, both announcement times are treated equally in this thesis.

Variable utilized in this research are days. As companies studied in this thesis are some of the largest in Nasdaq Helsinki, only major M&As in terms of value are analysed. Each stock price and index value are standardized to 100, which represents their value at the time of *t*. This is done so comparisons are easier to make.

As mentioned before, all represented data was collected by utilising Bloomberg Terminal, unless mentioned otherwise. Only mergers and acquisitions are studied, divestments are disregarded. Another requirement is announcement of price paid. As such, some of the largest Finnish companies are not part of this thesis.

4 Empirical results

In this chapter, biggest M&As of Finnish companies are presented. Their stock prices are compared to HEX25 index. Case companies are presented in blue colour, whereas HEX25 is coloured orange. As mentioned in chapter 3, each stock price and index value are standardized to 100, which represents their value at the time of t. Data labelled values present *t+1*, *t+5* and *t+month*.

After all results have been presented, hypotheses presented in chapter 2 will be answered in chapter 4.2. Special attention is given to differences and similarities between outcomes of M&As of chosen case companies. These companies represent a wide array of different segments of Finnish stock exchange, ranging from e.g. industrial companies and telecommunication companies to insurance companies.

4.1 Results

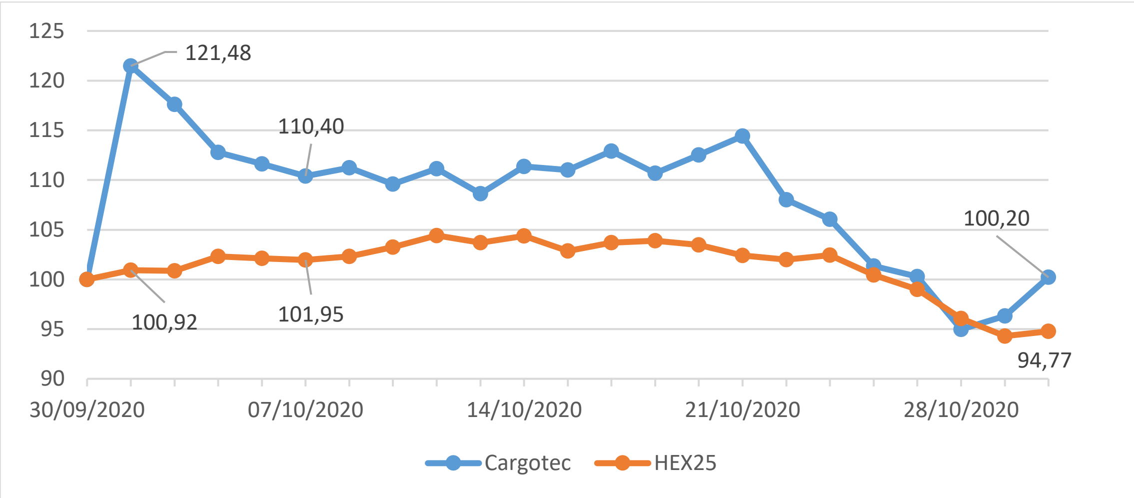

Figure 4 – Cargotec & HEX25, 10/2020

On 1st of October 2020, it was announced that Cargotec will merge with Konecranes (Cargotec 2020). Deal value exceeded 5,4 billion euros. On the announcement day, stock price of Cargotec increased by 21,48% compared to 0,92% of HEX25 (Figure 4), thus overperforming by 20,37%. On the fifth trading day, Cargotec and HEX25 were up by

10,40% and 1,95% respectively. As such, Cargotec overperformed by 8,29%. Finally, one calendar month later, Cargotec was still higher than HEX25, finishing at a gain of 0,20%, whereas HEX25 lost 5,23% of its value. As such, Cargotec outperformed HEX25 by 5,73% during this time period.

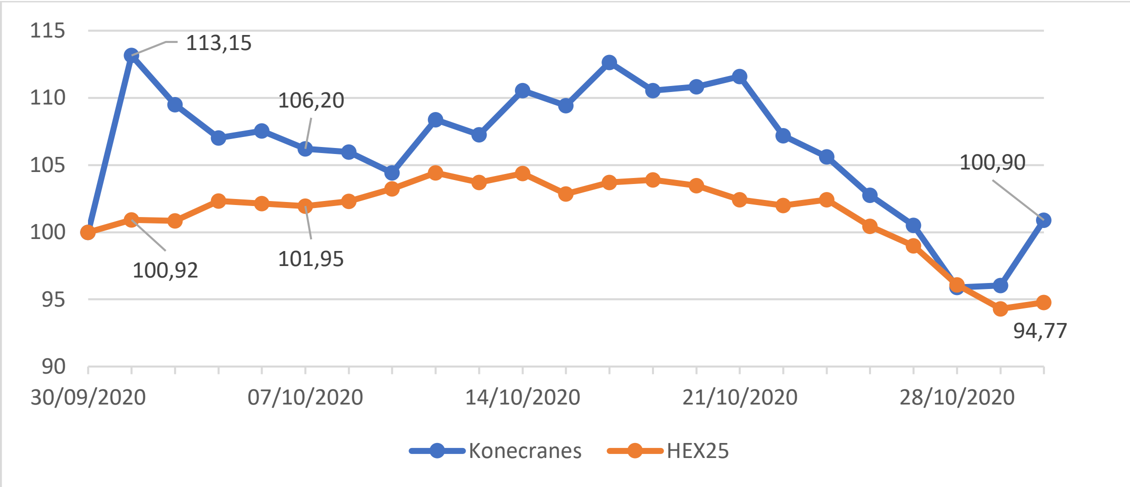

Figure 5 – Konecranes & HEX25, 10/2020

Figure 5 is also representative of the same Cargotec – Konecranes merger announcement, but instead researches stock price of Konecranes. Konecranes also received a substantial boost on the announcement day, as it closed at +13,15%, overperforming HEX25 by 12,12%. Following the same pattern of Cargotec, on the fifth trading day it was still up at 6,2% but was closer to the level of HEX25 which was at 1,95%; Cargotec outperformed HEX25 by 4,17%. At the end of the month, it was up by 0,90%, thus outperforming HEX25 by 6,46%.

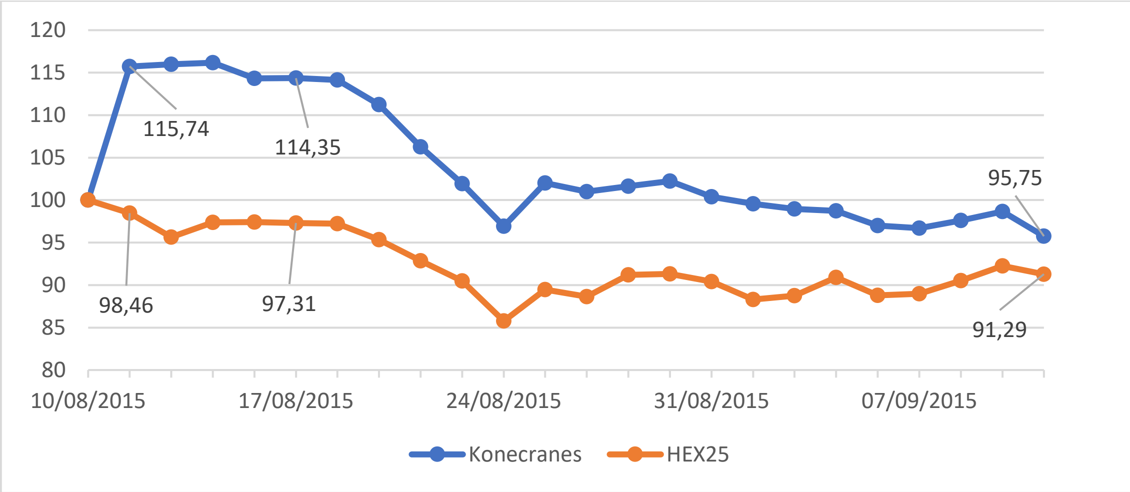

Figure 6 – Konecranes & HEX25, 8/2015

On 11th of August 2015, Konecranes announced its merger with Terex (Konecranes 2015). Deal value was 3,8 billion euros. Even though it was a negative day in general at Helsinki, Konecranes enjoyed a climb of 15,74%, outperforming HEX25 by 17,55%. After the fifth trading day, Konecranes continued to clearly outperform HEX25, this time by 17,51%. After a month, stock price had fallen below its starting point. However, Konecranes still outperformed HEX25 by 4,89%. (Figure 6)

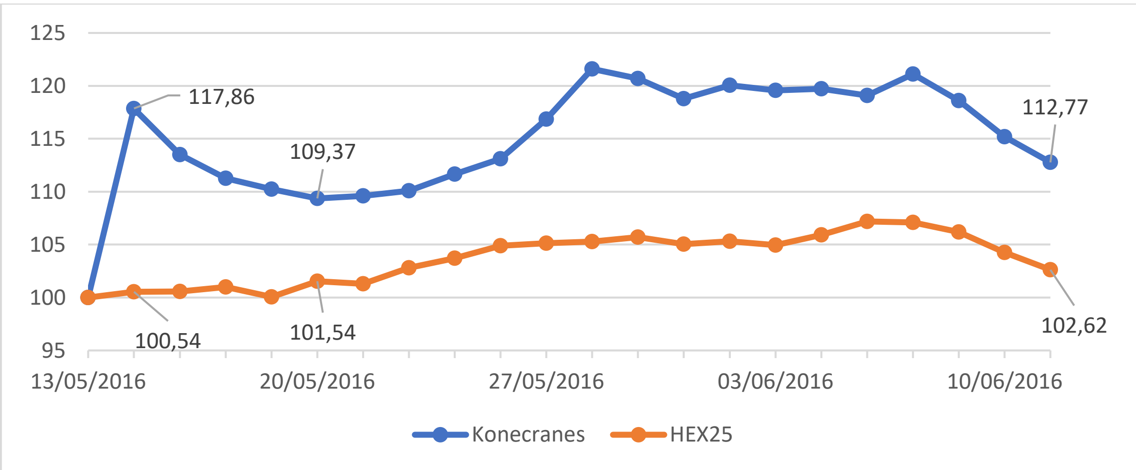

Figure 7 – Konecranes & HEX25, 5/2016

On the morning of 16th of May 2016, Konecranes announced acquisition of Terex's Material Handling & Port Solution business (Konecranes 2016) for 1,2 billion euros. On announcement day, stock price soared 17,86%, outperforming HEX25 by 17,23%. On the fifth trading day, stock price was still up by 9,37% whereas HEX25 was modestly up by 1,54% which meant that Konecranes was outperforming by 7,71%. At the end of the calendar month, Konecranes was up 12,77% while HEX25 climbed 2,62%. As such, Konecranes outperformed HEX25 by 9,89% over the month. (Figure 7)

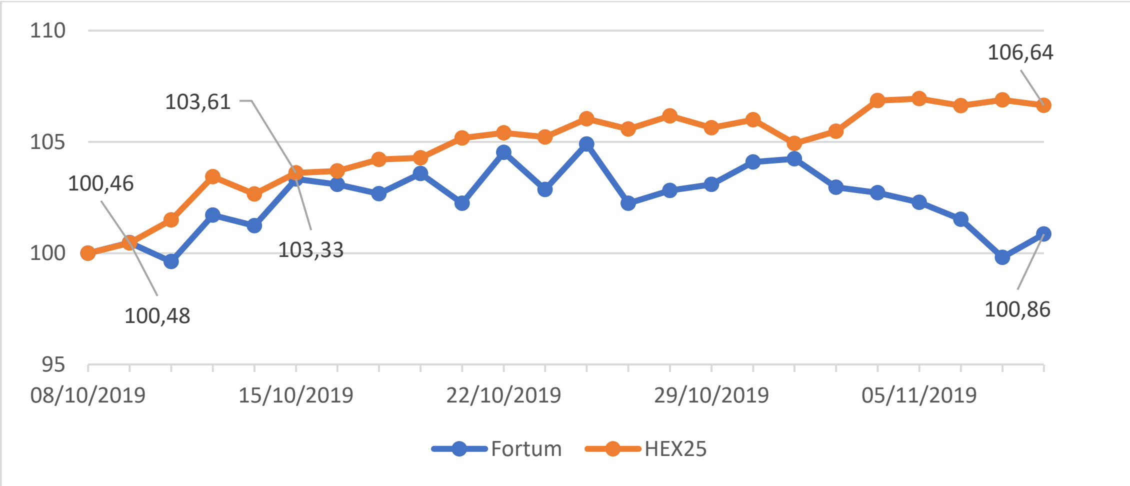

Figure 8 – Fortum & HEX25 10/2019

In October 2019, Fortum announced that they have become a majority shareholder of Uniper in a deal worth 4,2 billion euros. Following the announcement, stock price reaction was modest; Fortum outperformed HEX25, but only by 0,2%. After five days, the situation remained similar, this time Fortum underperformed HEX25 by 0,27%. After a month, however, the underperformance widened and was at 5,42%. (Figure 8)

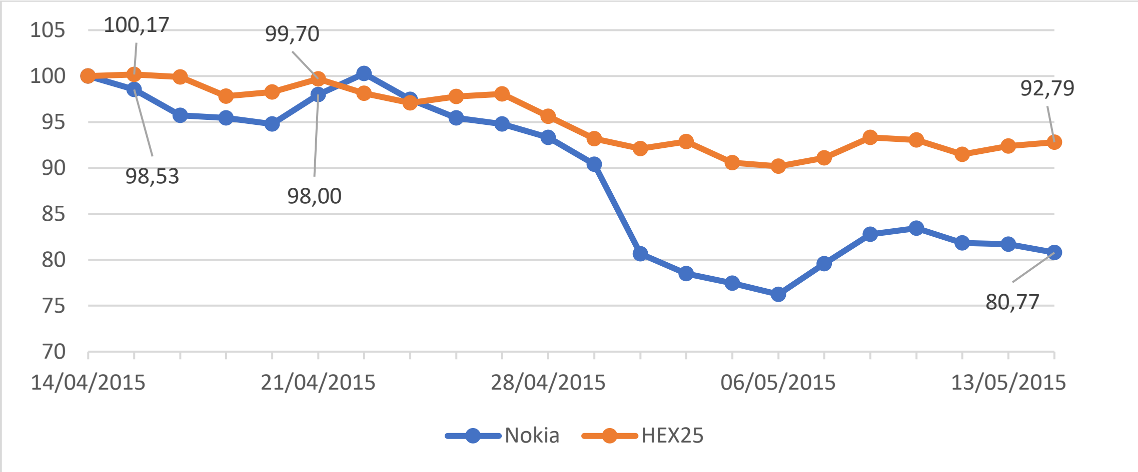

Figure 9 – Nokia & HEX25 4/2015

Figure 9 represents stock price performance of Nokia after its acquisition announcement of Alcatel Lucent. It is the biggest transaction performed by a Finnish company; total value exceeded 10 billion euros. Following the announcement, Nokia's stock price began to slip. On announcement day, Nokia's price fell and it underperformed HEX25 by 1,64%. After the fifth trading day, underperformance continued; this time by 1,70%. By the end of the month, underperformance intensified. Nokia had lost nearly 20% of its stock value in a month, while simultaneously underperforming HEX25 by 12,95%. (Figure 9)

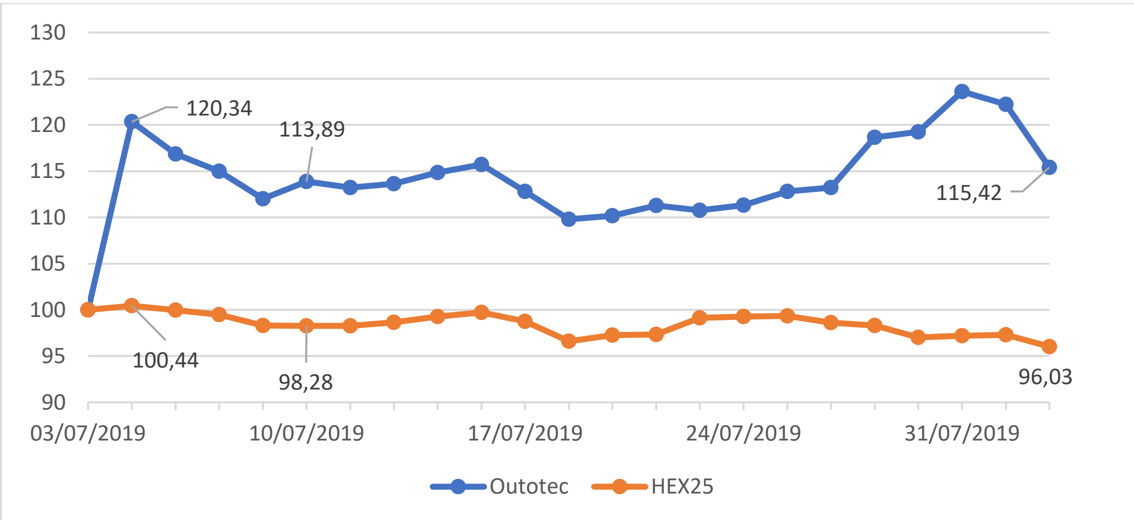

Figure 10 – Outotec & HEX25 7/2019

In July 2019, Metso and Outotec announced their merger. Deal value was announced at 2,7 billion euros. Figure 10 represents stock price of Outotec following the announcement. After the announcement, Outotec soared 20,34%, outperforming HEX25 by 19,81%. Five days later, Outotec continued its outperformance over HEX25, this time by 15,89%. By the end of the month, Outotec outperformed HEX25 by 20,19%. (Figure 10)

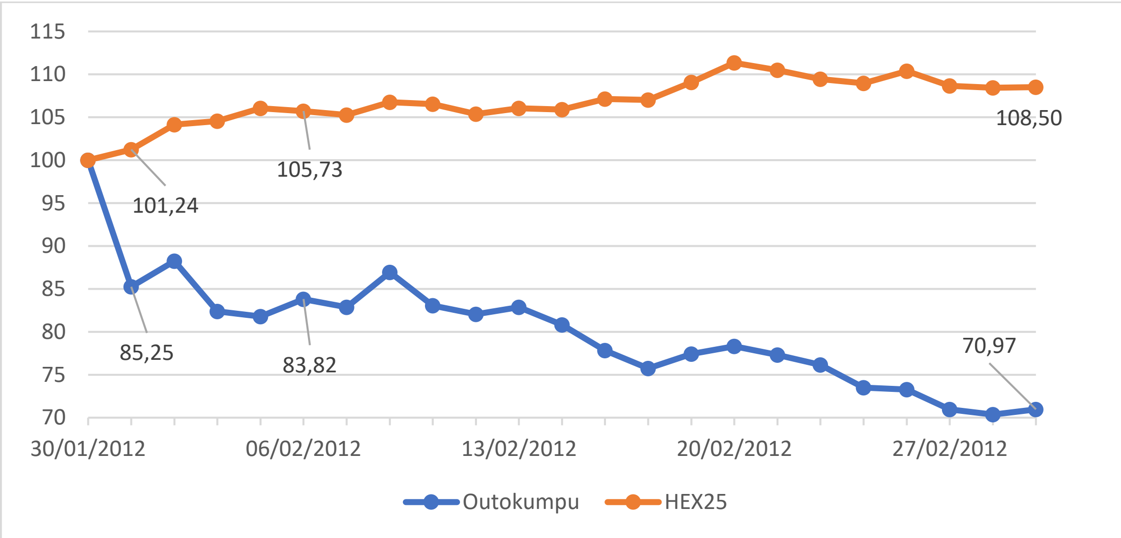

Figure 11 – Outokumpu & HEX25 2/2012

In January 2012, Outokumpu announced that it will acquire Inoxium from ThyssenKrupp in a 2,7 billion deal. Since then, only three deals performed by Finnish companies have been bigger. After the announcement, stock price of Outokumpu plummeted. Following the announcement, stock price slid by nearly 15%, underperforming HEX25 by 15,80%. This trend continued throughout the month, as Outokumpu underperformed HEX25 after five trading days by 20,72%. After a month, nearly 30% of the stock price has been lost. At the same time, Outokumpu underperformed HEX25 by 34,59%. (Figure 11)

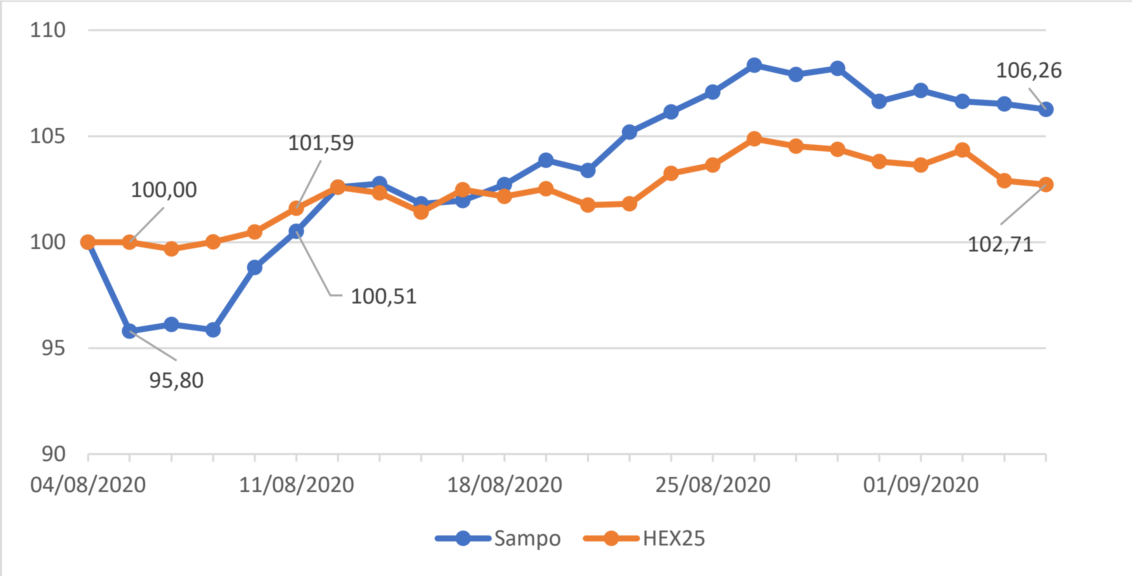

Figure 12 – Sampo vs HEX25, 8/2020

In August 2020, Sampo announced that they have become a majority shareholders of Hastings in a deal worth 1,4 billion euros. Following the announcement, stock price of Sampo fell and it underperformed HEX25 by 4,20%. After five days, Sampo had recovered but was still slightly underperforming HEX25, this time at 1,07%. After a month, Sampo had gained traction and was outperforming HEX25 by 3,46%. (Figure 12)

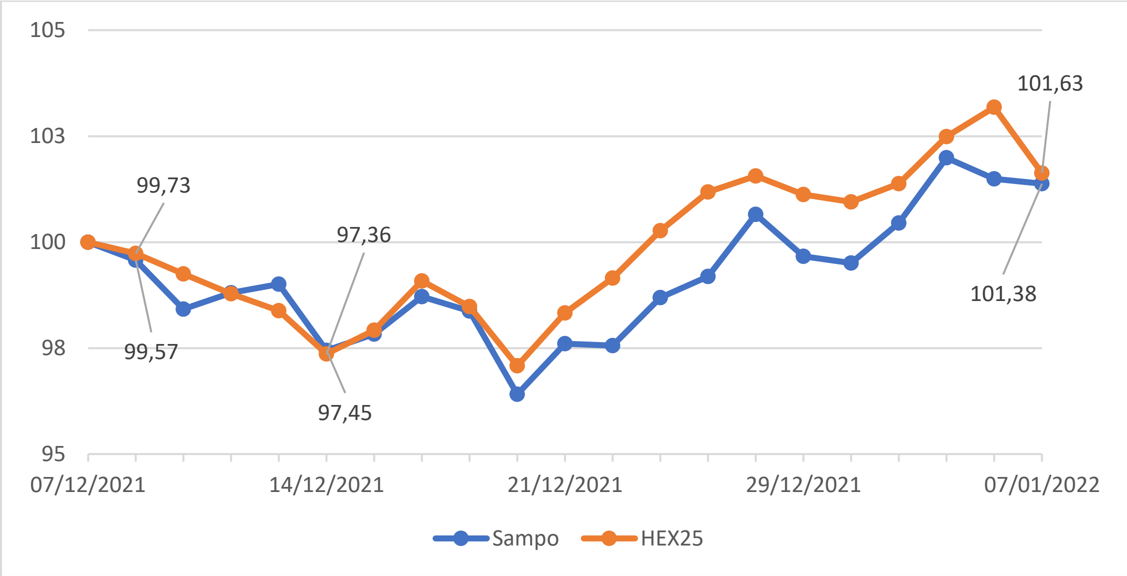

Figure 13 – Sampo vs HEX25, 12/2021

In the next year, Sampo announced that they have acquired full ownership of Hastings. Following the announcement, Sampo underperformed HEX25 by 0,16%. On fifth day, Sampo just beat HEX25, by 0,09%. After a month, it remained its very close proximity of HEX25, finishing by underperforming HEX25 by 0,25%. (Figure 13)

4.2 Summary of results

Figure 14 represents average progression of all case companies and OMX25 during the chosen time frame. On average, the trend is clear: initial euphoria boosts the stock price during the first trading days. As such, they outperformed HEX25 by 6,5% on the first day. But after euphoria begins to fade, stock prices revert towards OMX25. At the end of chosen time period, case companies underperformed HEX25 by 0,8%.

Based on Figure 14 and results presented in previous sub chapters, we can give answers regarding our hypotheses. H_1 is confirmed, as *t+1* had the biggest day-to-day swing over examined time period. When going into more detail, some companies enjoyed overperformance of over 20% compared to HEX25, thus creating substantial value for their shareholders. There were, however, also swings into other direction with highest underperformance compared to HEX25 at over 15%. Presented results prove that volatility increased considerably on *t+1*, in accordance with H_1. Even though case companies began regressing immediately after *t+1*, value creation for shareholders was substantial. Active shareholders had a possibility to realize sizable profits by selling immediately after the M&A announcement.

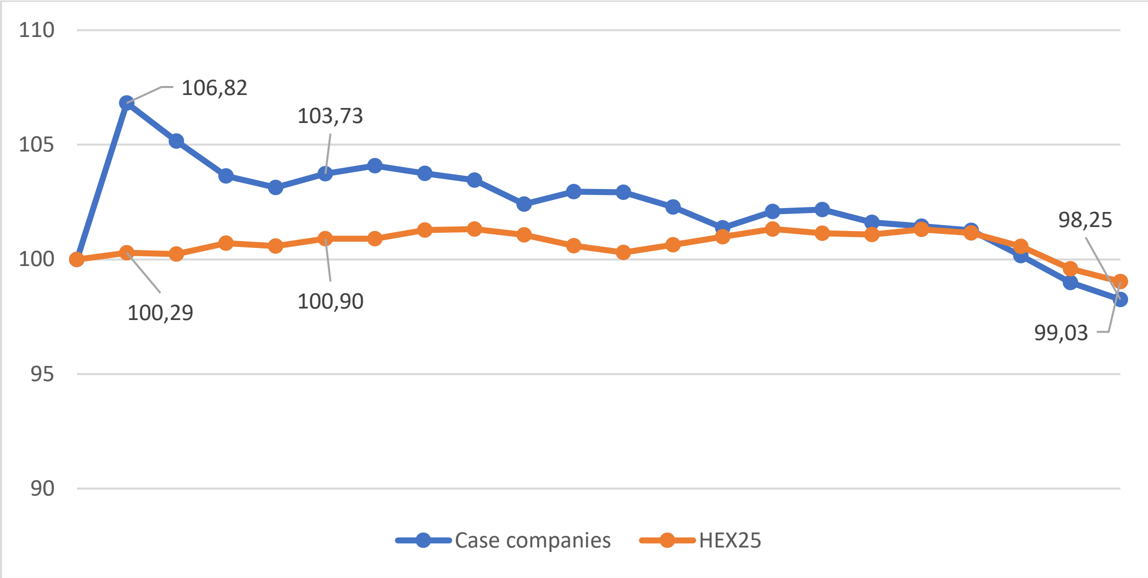

Figure 14 – Case companies vs HEX25

H_2 is partly confirmed and partly rejected. According to theory, acquiring companies do not create value for their shareholders. In this thesis, that is correct when looking at the whole time period. However, at *t+1* and *t+5* case companies outperformed HEX25 by a considerable margin, thus creating value for their shareholders. Even though trend line was downward after the initial euphoria at *t+1*, it must be noted that case companies were able to outperform HEX25 for nearly the whole time frame, only dropping below HEX25 for the last 3 days.

As the situation regarding created value for shareholders changes throughout the month, it is crucial to note that shareholders should recognize their own importance in value creating process. They can reap the possible rewards made possible by M&A announcement, but the time window is limited. By waiting too long, profits will vanish. Reacting at the earliest possible time is key in realizing profits. As such, active investors will have advantage over their passive counterparts.

In total, the data set utilized in this thesis demonstrates some clear similarities of stock price movements between chosen companies. When examining only those companies who outperformed HEX25 on *t+1*, there is a clear pattern of reverting back towards HEX25. This is presented in Figure 15.

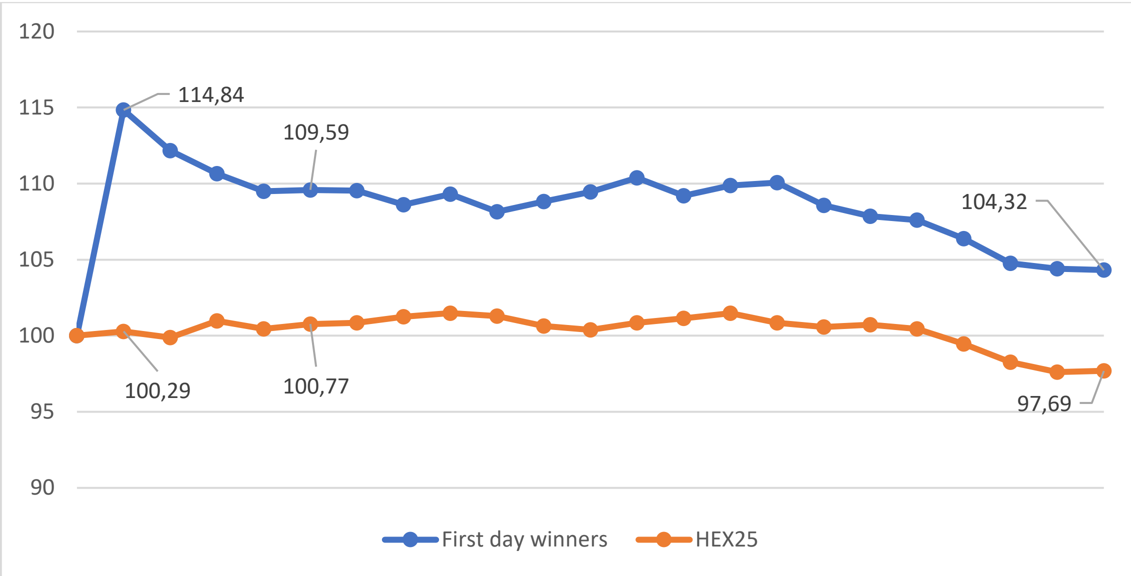

Figure 15 – First day winners vs HEX25

Even though first day winners continue to clearly outperform HEX25 over this time period, it is evident that shareholders would gain most profit by selling during the first trading day after the announcement. After the first day, profits start to dwindle. By selling on the first day, shareholders beat HEX25 by 14,5%. However, if they wait a month, they only beat HEX25 by 6,8%.

Figure 16 represents stock price progression of those who underperformed compared to HEX25 over a time period of one month.

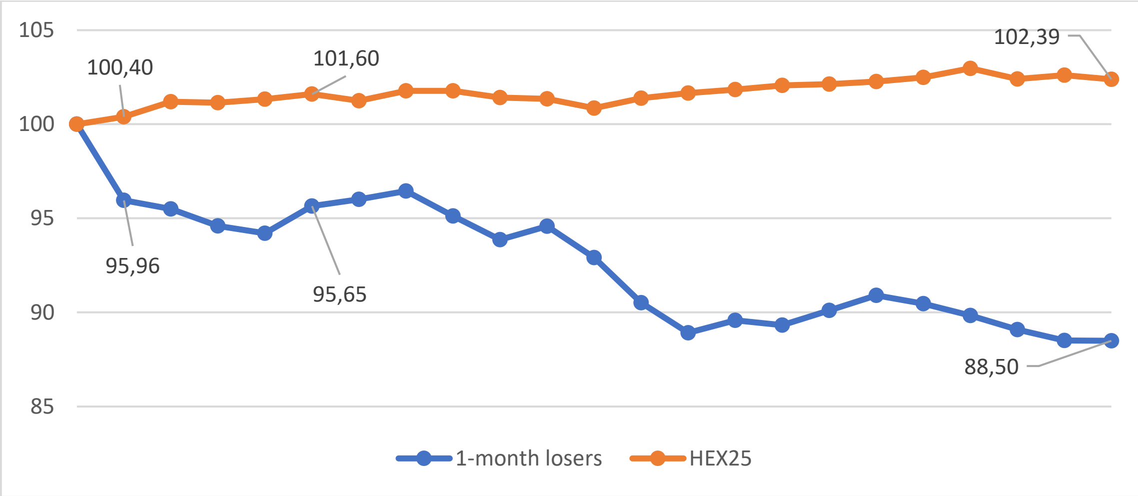

Figure 16 – 1 month losers vs HEX25

Trend line for these "*1-month losers*" is clear; the situation is only getting worse over time. As such, shareholders can minimize their losses by reacting quickly to unfavourable M&A announcements and cut their losses on announcement day.

There is one striking similarity between both winners and losers. In both cases, on average, shareholders maximize their profit by selling their stocks following the M&A announcement, which means selling on *t+1*. In both cases, *t+1* is the best date to sell, followed by *t+5* while *t+month* is the worst of the three chosen reference points.

In addition, it can be noticed that stock market does not change its opinion easily after the initial reaction. This is evident in the data set, as 80% of the companies finished the month how they started it. In only 20% of cases underperformance compared to HEX25 on *t+1* was turned into outperformance on *t+month* or vice versa. When taking into consideration how profits are at their highest on *t+1*, practical and logical shareholders should always sell their shares on that day. There may be e.g. tax-based reasons for not selling, but for those shareholders who are aiming to maximize their short term profit, the only correct conclusion of this thesis is to sell on *t+1*.

When disregarding averages and their comparison to HEX25, and looking at case companies on individual level, in 70% of cases *t+1* was the most profitable selling day. In 30% of cases, *t+month* was the most profitable one, suggesting that initial reaction on *t+1* was perhaps too strong. After a month of studying how M&A truly effects the company, sentiment had changed on those cases. Even so, such cases were in minority, as *t+1* was the most profitable day to sell in most cases.

To further emphasize importance of selling on *t+1*, Figure 17 demonstrates how case companies and HEX25 develop from *t+1* to *t+month*.

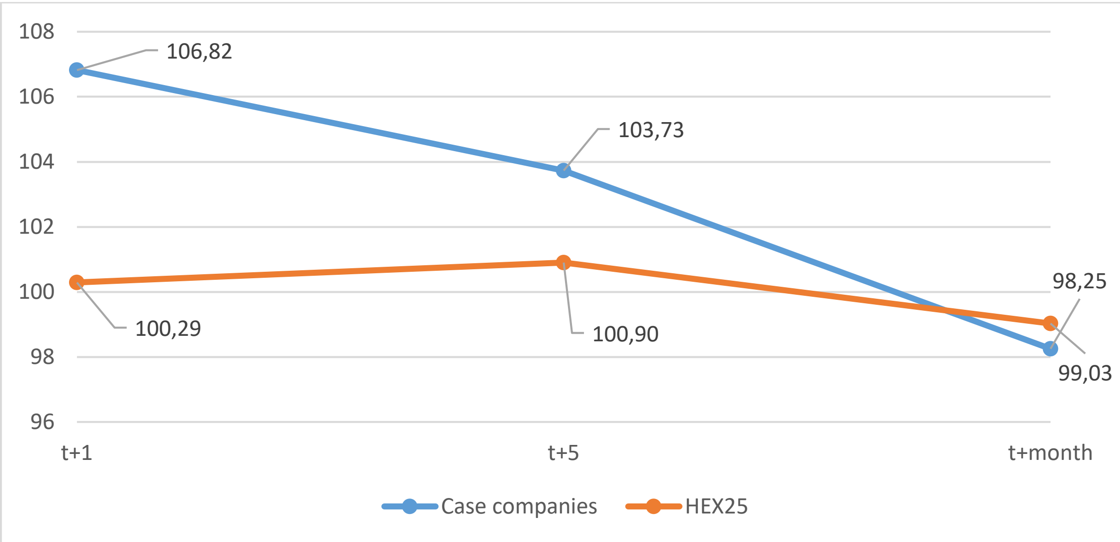

Figure 17 – t+1 to t+month

Situation becomes even more obvious when analysing how case companies perform against themselves at t+1. Over this time period from *t+1* to *t+month*, HEX25 lost 1,26% of its value. However, case companies lost 8,02% of their value during the same time frame. Thus, the difference between the two was 6,77 percentage points with case companies being clearly worse investments than HEX25.

To summarize all results, this thesis proves that companies can create value for their shareholders. However, there is a clear point in time where profits are at their maximum, which is on the day following the announcement. Even though it may be due to overly positive initial reaction creating an imperfect valuation of a company, the fact remains that shareholders can utilize M&As to their own benefit, especially on a short time period. When looking at figures and data presented in this thesis, it can be argued that value is created only once – on the announcement day. After the first trading day, trend line starts to point downwards, thus destroying value each day. As such, reaction time is key, and this thesis supported by its data recommends those seeking maximum short-term profit to sell their shares on the first day following M&A announcement as it is the most profitable strategy.

5 Discussion and conclusions

M&As are carried out in order to create value for shareholders (Sudarsanam 2010; Colman & Lunnan 2011). At the same time, popularity of M&As as a strategy has grown and they represent a viable way to grow the company (Weber & Drori 2011). However, according to King et al. (2004), M&As, especially on longer time frame, do not create value for shareholders.

This thesis examines if companies can create value for their shareholders through mergers and acquisitions on a short time frame, spanning a period of one month. The empirical part of the research examines how case companies performed against OMX Helsinki 25 (HEX25) index over the chosen time frame. This was done to nullify impact of possible global shockwaves to stock markets and enable to measure over-/underperformance against HEX25 index. The data was collected utilizing Bloomberg Terminal. In order to get meaningful results, data was restricted to include only the biggest M&As of Finland over the last 10 years. This was done to maximize impact of M&A announcement to stock price.

With the achieved results of this thesis, we can answer research question, which was:

1) Can companies create value for their shareholders through M&As?

As was presented in chapter 4, companies can create value for their shareholders by engaging in M&As. This thesis studied stock prices following the biggest M&As executed by Finnish companies, and it was proven that on average, M&As offer great possibilities for shareholders to benefit from them. Even though after a period of one month, the companies engaging in M&As were underperforming HEX25 (thus destroying shareholder value), the initial reaction to merger or acquisition announcement was noticeably positive. Shareholders, however, must be active to maximize their profit as the first trading day following the announcement is the best day to sell shares. Passive investors did not benefit from M&As during this time frame, so the recommendation for them is investing in indices. For active investors, however, the recommendation is to sell on the first possible day following the announcement, if e.g. possible taxation is a non-factor.

To support the primary research question, secondary research questions are:

2) What is the initial reaction of stock market following the M&A announcement?

Secondary research question can be answered by analysing the research provided in this thesis. Initial reaction to M&A announcement was, on average, strongly positive. Reaction on the first day was volatile, as stock prices were swinging from 20% overperformance to 15% underperformance. On average, the initial reaction of case companies was clearly positive, outperforming HEX25 by 6,5% on the opening day.

3) How stock prices develop after initial reaction?

This secondary research question allows us to examine the situation once dust has settled. Results collected in this thesis show that companies engaging in M&As, after the first trading day following the announcement, are not able to keep positive momentum. In fact, when analysing the time frame from second trading day forward, value is lost at a very substantial pace compared to HEX25.

With the help of primary research question and two secondary research questions, we can conclude that M&As do create value for their shareholders. However, time window for shareholders to realize this value creation due to M&A announcement is very short. Research shows that on average, investors seeking to maximize their short-term profit should sell their stocks on first day possible. Holding on for examined shares in this thesis after the first trading day is a value destroying decision by shareholders.

As a conclusion, active investors are more likely to benefit from M&As than their more passive counterparts. As such, active investors may utilize M&A announcements to their benefit by selling their own shares of acquiring company. Another way to benefit is engaging in short selling of said company after the initial euphoria begins to fade. Based on results of this thesis, both actions have positive expected outcome.

Even though they were not directly analysed in this thesis, there are two major Finnish companies which are interestingly and distinctively different from other HEX25 companies. As mentioned in chapter 3, both Kone and Neste have a clear policy of not announcing prices they have paid for acquisitions. As such, short-term analysis of their stock price reactions to M&A news were impossible to make. It is interesting to speculate why they have chosen this strategy, and one clear difference between them and other HEX25 companies is concentrated ownership; Finnish Government has majority ownership in Neste, whereas Herlin family holds ruling control of Kone. As such, they may not see reason to be transparent, because as major owners, their control of their companies is absolute. However, there appears to be an additional reason for their approach. Research has proven that companies who are more secretive during M&As outperform their more open and transparent counterparts by nearly 10% in the long-term comparison, partly because they can retain their competitive advantage better, and keep their competitors guessing (Guo, Li, Hu & Wang 2019). As a result, suggestion for future research could be doing comprehensive research, perhaps by utilising qualitative approach and interviewing key executives and managers of Kone and Neste. These interviews could help understanding why they these companies have aforementioned policies of secrecy regarding M&As. Simultaneously, their long-term stock price performance should be measured against other companies and/or indices.

Even though this thesis did not aim to measure long-term performance, suggestion for future research is to do a deeper analysis how transparency, or lack thereof, in M&A announcements influences value creation for shareholders of Finnish companies on a longer time frame. In addition, as case companies of this thesis evidently started to underperform against HEX25 after the first day, a suggestion for further research is studying if short selling of companies after M&As increases, as there are appears to be profits to be made.

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