Analysis on Human Resource Risk Management in Cross-border Mergers and Acquisitions

Yao YAO*
Hangzhou Institute of Service Engineering, Hangzhou Normal University, Hangzhou, China
yyaoexist@163.com
*Corresponding author

Keywords: Human resource, Cross-border mergers and acquisitions, Risk management.

Abstract. As an emerging economy undergoing structural reform, employment quantity and quality in China benefit from outward foreign direct investments. Cross-border mergers and acquisitions have been developing rapidly. International human resource integration is one of the determining factors in the success of the outward direct investment. Human resource management risk is more complicated in the situation of cross-border mergers and acquisitions. With case studies from cross-border merger and acquisition practice in China, this paper studies the risks in cross-border mergers and acquisitions, and gives corresponding coping strategies. Human resource management risk has various forms in cross-border mergers and acquisitions, arises from various source, such like labor risk, cultural difference, organizational cultural divergence, incentive system. This paper analyzes strategies for international human resource management, include localization strategy, social responsibility of multi-national corporation in host country, communication, incentive reward system and due diligence before merger and acquisition.

Introduction

Follow the “going out” policy, outward foreign direct investment surged over the past decade. Greenfield investment and cross-border mergers and acquisitions are two most common methods adopted in foreign direct investment. Cross-border mergers and acquisitions plays more and more important role in outward direct investment, which could acquire asset from existing foreign corporations, include intangible asset such as brand, trademark, copyright or patent. Through cross-border mergers and acquisitions, investors can benefit from reverse technology spillovers, make full use of expertise, technology and management experience. Cross-border mergers and acquisitions attract investors more favorable than green field investment, in the aspect of regulation compliance and local acceptance. The scope and scale of cross-border mergers and acquisitions is expanding. Human resources management comprises crucial part in modern corporation management. Tank of talent, skilled workers contributes to efficiency, profitability and aggregate competitiveness in a corporation. In the circumstance of merger and acquisition, human resource integration is one of the determinant factors in success of the investment, especially in an international direct investment. Cultural distance between home country and host country, different organization culture between the investor and the target, different labor law system, the afore said risk factors can all lead to uncertainty in human resources integration in cross-border mergers and acquisitions, which in turn influence the
performance of the new firm, and the profitability of the investor from home country. This paper analyzes human resource management in the background of cross-border mergers and acquisitions. The paper is structured as follows: the first section gives an introduction of cross-border merger and acquisition and human resources management, the second section address risks in human resource integration in the process and aftermath of cross-border mergers and acquisitions, the third section gives risk mitigating strategies, and the last section gives conclusions and policy implications.

**Risks in Human Resources Integration**

**The Labor Risks.** The working ethics and labor legislations are quite different between countries. The countries with strong union have higher degree of uncertainty. Employees in developed countries enjoyed high salary and good benefit system, which indicate that labor risk raise when a corporation from developing country invests in developing countries. The failure of SAIC Motor’s acquisition of SSang Yong Motor in Korea is an example of labor risk. The unexpected high labor cost from SSang Yong Motor, the hostile attitude from SSang Yong employees, the persisting strikes, drove the investment to the drain. The trade union risk is prevailing in Latin American counties and other regions. The investment of Shougang Group in Peru is the result of union risk. The persistent strikes and repeated increasing salary by the trade union lead to high labor and legal cost, which in the end lead to the failure of the cross-border acquisition. Shougang Group is not alone. In resource seeking outward direct investment from state owned enterprises of China, labor risk is prevalent. Union risk, strikes, salary raising required, refusal to overtime, are all the factors need to take into consideration in the decision making process in cross-border merger and acquisition. The diversified labor law compliance also need consideration.

**Cultural Risk.** Cultural risks arise while cultural distance in religion, history and way of thinking is different between home country and host country. As for risk management process, risk identification and measurement comes before management and control. However, cultural risk is difficult to identify and quantify. Hofstede's cultural dimensions theory can be applied to measure cultural risk in international merger and acquisition. The cultural distance between countries is measured by follow five dimensions in the theory of Hofstede, that is, power distance, uncertainty versus avoidance, individualism versus collectivism, masculinity versus femininity, long term versus short term, and later indulgence and constraint is also added into the theory. Based on thorough and extensive investigation and research, the cultural distance dimensions gives an aggregation quantified measurement of cultural distance, which can be used as objective variable in managing cultural risk. As for the dimension of power distance, some countries may not have the same degree of respect to authorities, nor do they take order from individual executive, discipline employees as in domestic companies may not be reasonable. As for the dimension of uncertainty, when a Chinese company acquired an old establishment in Europe with long history, the old employee may not be able to adapt to our way of regressive development. As for the dimension of individualism, some western countries value personal opinion more than collective wisdom. As for the dimension of long term versus short term, some corporations acquire a foreign corporate for immediate gain, which could lead to employee’s discontentment. As for indulgence and constraint, in countries with higher level of indulgence, overtime work which is prevailing in domestic labor market, may cause
dissatisfaction or even strike in host countries. Divergence in religious and cultural convention is another source of uncertainty, respect and adapt to the tradition of staff in host countries is an important issue in international human resources management. The tradition of religion in Saudi Arabia contributes to the failure of the project by China railway construction corporation. The misunderstanding and mistrust due to religious belief lead to strikes and difficulties in construction. Nationalism risks existed in countries which has conflict with investment country in history, or has a general hostile attitude towards investment country. In some countries in Southeastern Asia, emotions against China could lead to strike, or even vandalism or other violent behavior.

Organizational Culture Divergence. The corporations usually establish their own organization culture during their business activities, from the notions of the leadership, the location of the corporation, the characteristic of the industry and the business environment it operates in. There could be large gap in organization culture between different corporations. The employees from the target corporation may not accept the investor’s organization culture without impediment. BenQ corporation’s acquisition of Siemens result in bankruptcy, one of the reasons is that the Siemens employees’ inability to adapt to the profit driven culture of BenQ corporation. As an enterprise with long history, the organizational culture of Siemens emphasize on tradition and high standard of quality. While fast developing BenQ emphasizes expansion, risk taking and immediate profit-seeking. The acquisition of IBM by Lenovo China is considered a relatively successful cross-border acquisition of China. For Lenovo combined the organizational culture of Lenovo with IBM. The IBM staff was invited to make new organizational culture in the newly reformed firm. The Geely Auto Group include Volvo employees in decision making in the new corporation, which lead to smooth integration in the merger and acquisition.

Difference in Salary Structure. The reward system which mostly embodied in the salary and payment system is one of the determinant factors in success in international human resource integration. Combination of efficiency and equality is crucial in salary structure design. How to balance incentives and economic security, so as to encourage the employees is an important issue in human resources management, domestically or internationally. Cost control and salary payment could be contradicting, weighing between them could determine the performance and profitability of the new corporation. Various reward instruments, which may not be common in China’s labor market, could be prevailing in overseas target corporations, such as employee incentive options, paid leave, etc. The benefits and subsidies are more complex as well, which could be more than expected. The acquisition of Alcatel by TCL illustrated human resource loss due to difference in salary system. Larger numbers of Alcatel resigned after the acquisition, despite high labor cost of TCL into Alcatel. Most of the investment funds from TCL became labor costs. The financial burden caused layoffs, which in turn makes more labor problem.

Strategies in International Human Resources Management

Localization. Localization of employees, especially higher proportion of local staff in management, have positive effect in communication between investors and host country employees. The integration of organizational culture calls for the participation of the local employees. The strategy of localization in human resource management works more efficiently
as part of general localization strategy. It could be combined with localization of product, marketing, culture, research and development. Integration into local social economic situation and local culture, provides more managerial position for local employees, would reduce cost in human resource, make full use of the expertise and skills in the target corporation.

**Social Responsibility.** Enhancing the role of social responsibility of enterprises is key. Huawei technology limited has been conducting business all over the world. Its branches and affiliates are established globally. To mitigate human resource management risk, a department is designated the task of social responsibility. The department of social responsibility can help Huawei technology limited to build a positive image. The activities, such as donation in local schools and hospitals, relieve the tension between local residence and foreign company, and increase the degree of acceptance of the local employees. Especially, for state owned enterprises, the enterprise represents the image of the country, while building confidence and creditworthiness would be even more important.

**Communication.** Misunderstanding and distrust resulted from cultural differences can be solved by effective communication. For corporations in merger and acquisition, communication and coordination is required before, during and after the process. Effective communication contributes to efficiency and cohesion. Cultural, linguistic and religious difference, makes human resources management more difficult in the case of cross-border mergers and acquisitions. Language problems and different way of thinking impedes efficient communication. The staff from host country and home country needs to respect each other, respect their tradition and culture. Cross cultural communication skills is required in management staff in multi-national enterprises. Inclusiveness in decision making in mergers and acquisitions can also help ease the tension, collect more suggestions from host country employees, which would give incentives to local and foreign staff, and in turn reduce the difficulty in human resource integration. Effective communication would increase the understanding of the employees to the new enterprise, enhance their sense of belonging, minimize their sense of anxiety and uncertainty, and provide a positive organization atmosphere.

**Due Diligence.** Due diligence concerning the host country and the target corporation would be necessary before cross-border mergers and acquisitions. Due diligence should become a regular process in decision making process for cross-border mergers and acquisitions. Investigation of the host country, include culture, the labor law, the business convention, needs to be researched and analyzed. Investigation of the target corporation, include the structure of the staff body, trade union, the cost of salary, benefit and pension, etc. lack of proper due diligence attributes to the human resource risks in some less successful cross-border mergers and acquisitions cases. Human resources planning for the new enterprise need to be carried out before the merger and acquisition. The characteristic of the industry and the business, the structure of human resources in both corporate, the demand and supply of human resource in the industry, the background of old employee, are all need to be included in due diligence report.

**Incentive Reward System.** Design a reasonable, cost effective and proper incentive reward system, upon agreement from all parties, include the investor and the staff, the management and frontline staff. The salary system should be applied to local legislations, regulations and other
rules. The design of the salary system should also in accordance with the development strategy of the new corporation. Reward system should include not only salary and benefits, but also opportunity of training and promoting. Self value realization would be more meaningful than just economic gains.

Conclusions

Cross-border mergers and acquisitions have been developing rapidly. The human resource management plays an important role in determining the success of the outward direct investment. International human resource integration is one of the factors influence investment. Human resource management risk is more complicated in the situation of cross-border mergers and acquisitions. With case studies from cross-border merger and acquisition practice in China, this paper analyzes the risks in cross-border mergers and acquisitions, and gives corresponding coping strategies. Human resource management risk has various forms in cross-border mergers and acquisitions, arises from various source, such like labor risk, cultural difference, organizational cultural divergence, incentive system. Labor risk arises from different work ethics and legislation, as well as the role of trade union. Cultural difference in language, religion, tradition, business convention, and consequent inefficiency in communication, enhances difficulty in international human resource management. Organizational culture which can be quite different, has impact in the atmosphere of working environment for employees. Different salary system could lead to high labor cost to investors, and dissatisfaction from local employees. This paper emphasized on some strategies for international human resource management, include localization strategy, social responsibility of multi-national corporation in host country, communication, incentive reward system and due diligence before merger and acquisition.

Acknowledgement

This research was financially supported by the Natural Science Foundation of Zhejiang Province, Research on financial time series data mining, LQ15F020013.

References


