

# The big exit: executive churn in the wake of M&As

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In 2003, *Harvard Business Review* published the results of the first author's initial research on top management team effects in M&As (Krug, 2003). He reported that M&As lead to long-term instability among target company top management teams. This finding was significant because previous studies had assumed that top management turnover rates, while high immediately after the acquisition, generally return to normal levels within two or three years after the acquisition. His research, however, indicated that M&As may create instability in target executive teams that lasts many years after the acquisition. Because research shows a strong association between executive turnover and poor post-merger performance, long-term instability among executive teams may be an important cause of merger failure.

These initial findings generated profound interest among M&A practitioners. In particular, they confirmed the real-world experiences of the second author. Two years ago, we began collaboration with other members of Accenture's Organizational Strategy Group on the issue of executive turnover following M&As. Our interest was to develop deeper insight into what happens to executives following an acquisition, how disruptions to leadership continuity in target companies might be minimized, and how new top management teams can be created to maximize the effectiveness of the merger integration process.

Our initial objectives were two-fold. First, we wanted to determine whether the top management turnover effects found in the first author's analysis of M&As from the 1980s held for M&As during the 1990s and 2000s. Second, we wanted to understand whether these effects held across a broad range of industries. A finding that M&A activity leads to similar patterns of executive turnover across different time periods and industries would imply that managing top management team integration is an important issue that should be addressed during consulting engagements involving the merger integration process.

We began by expanding the initial database to include representative samples of M&As in Accenture's primary industry groups, including financial services, securities, telecommunications, oil and gas, consumer goods, and retail, as well as manufacturing and service. This supplemental data collection consumed nearly two years. We analyzed close to 5,000 M&As to identify public transactions in the desired industry groups and time periods. The final database followed the careers of more than 23,000 executives in more than 1,000 target companies for 17 years surrounding the acquisition.

In total, roughly ten years have been spent compiling these data. Given the labor intensity and length of time needed for such an effort, it is highly unlikely that a comparable database will be compiled again in the near future. This creates a unique opportunity to generate deeper insights into a variety of top management team issues in M&As that can be leveraged to improve the effectiveness of post-merger integration engagements and improve top management team effectiveness.

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In this article, we provide a summary of preliminary findings that may be of interest to executives and consultants involved in the M&A process. We expect a variety of insightful findings to emerge as we continue to analyze these data and will report in future research notes and articles. A summary of the final database is shown in Table I.

### M&As destroy long-term leadership continuity in target firms

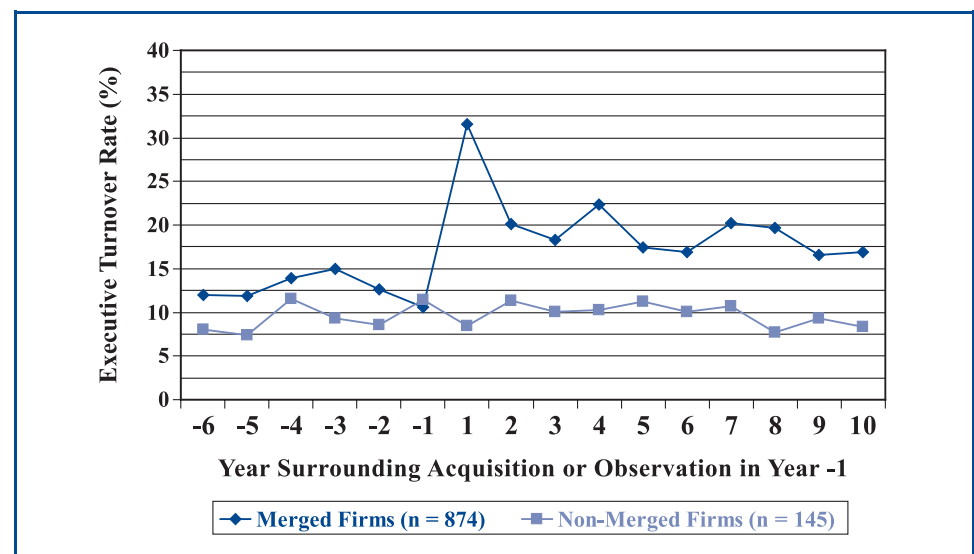
Figure 1 shows the trend in executive turnover rates for the 1,019 firms in the database. The blue line shows rates of turnover among executives in target firms acquired in year-1. The red line shows comparable turnover rates among executives in the non-acquired firms.

The merged firms experienced an average top management team turnover rate of 24.3 percent in each of the ten years following the acquisition. This compared to an average annual turnover rate of 12.1 percent prior to the acquisition. In contrast, the non-merged firms experienced an average annual turnover rate of 9.8 percent during the entire period of the study. Top management teams included an average of 9.7 executives.

T-tests were conducted to test for yearly differences in mean turnover rates between the merged and non-merged firms. In all ten years after the acquisition, the merged firms experienced significantly higher levels of turnover in their executive teams compared to the non-acquired firms ( $p < 0.001$ ).

Table I Database of target firms and executives				
No.	Industry	Targets	Executives	
1	Financial services	83	2,407	
2	Securities	18	508	
3	Telecom	52	910	
4	Oil and gas	66	1,331	
5	Consumer	178	4,332	
6	Retail	165	4,106	
7	Manufacturing	255	4,651	
8	Service	57	1,189	
	Mergers	874	19,434	
9	Control group	145	3,573	
	Total firms	1,019	23,007	

Figure 1 Top management turnover rates in the merged and non-merged firms (n = 1,019)



An examination of pre-merger turnover rates shown in Figure 1 suggests that merged firms also experience higher turnover rates prior to acquisition. In fact, *t*-tests do indicate differences in four of the six years leading up to the acquisition. After analyzing the data in greater detail, however, we found that 33 percent of the 874 target firms were acquired two or more times during the 16-year study period. When we exclude the effect of multiple acquisitions, any differences in turnover rates prior to the target company's acquisition in year-1 disappear (see Figure 2)[1].

These results show that most target company top management teams are relatively stable before they are acquired. This stability is similar to that experienced in firms that are not acquired. For the average firm, this leadership continuity is permanently altered once the firm is acquired. Target companies can expect to lose 21 percent or more of their executives each year – more than double that experienced in non-merged firms – for at least ten years after the acquisition!

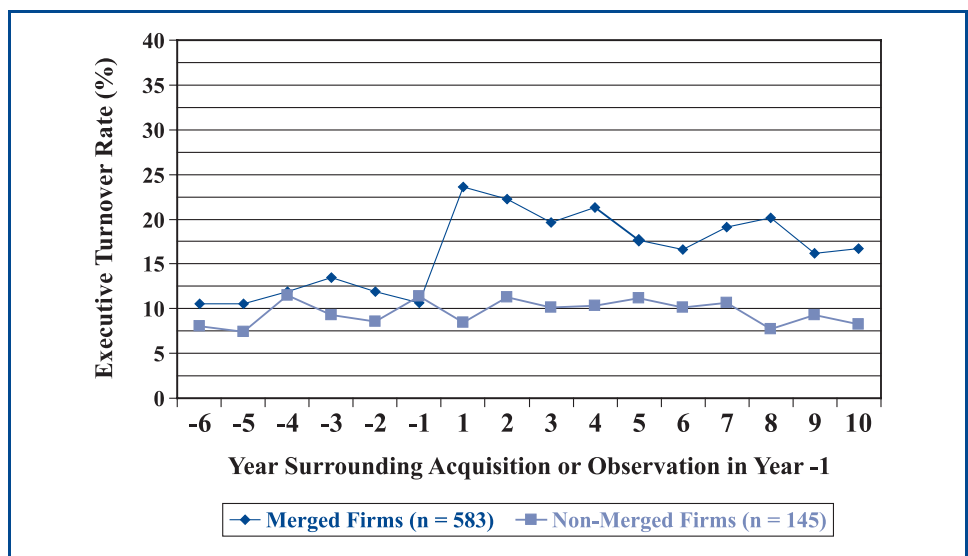
### What happens to executives in firms acquired more than once?

Figure 3 shows average annual executive turnover rates for those target firms acquired more than once (blue line) and the non-merged firms (red line). All 291 target firms were acquired in year - 1. Of these, 116 (40 percent) were also acquired several years earlier, while 175 (60 percent) were acquired several years later. The 116 firms previously acquired experienced significantly higher levels of turnover in each of the five years leading up to the acquisition in year - 1 (13 percent per year). Turnover rates stabilized in the year of the acquisition in year - 1, before rising again in year - 1.

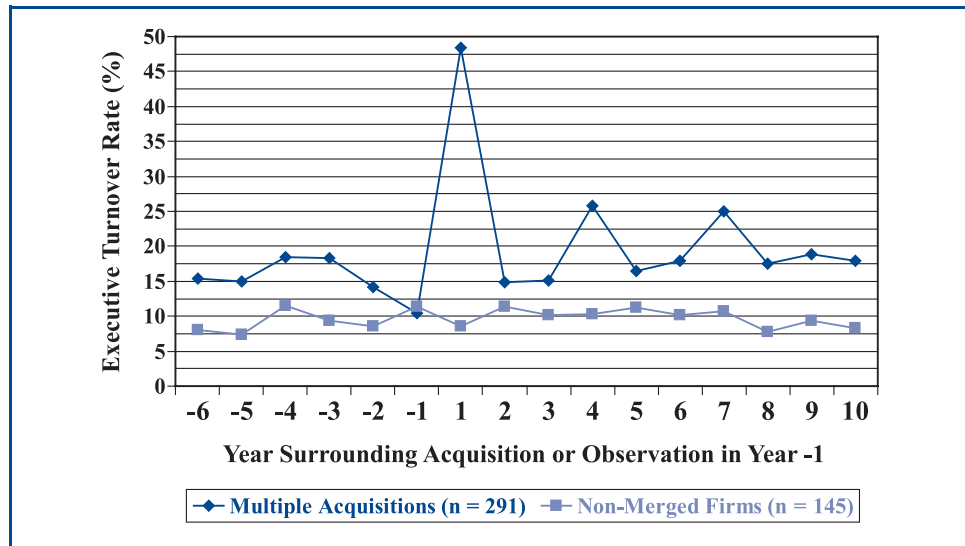
Firms that were acquired multiple times lost an average of 48 percent of their executives in the first year after the acquisition in year - 1. This compared to an average loss of 24 percent in firms acquired only once. During the ten years that followed the acquisition in year - 1, these firms lost an average of 32 percent of their executives in each year. This compared to an average of 21 percent in target firms acquired only once. Thus, firms acquired multiple times during a short period experience much higher and unpredictable rates of turnover among their executives than either non-merged firms or target firms acquired only once. The mass exodus of half of the firm's executives in the first year after the acquisition indicates that these acquisitions are quite different from other acquisitions.

What makes these acquisitions so much more unstable than other acquisitions? In many cases, failure of an earlier acquisition is the cause. Poor post-merger performance and unrealized synergy gains cause more than half of all M&As to fail. Up to one-half of all target

**Figure 2** Top management turnover rates in firms acquired only once in year-1 (*n* = 728)



**Figure 3** Top management turnover rates in firms acquired more than once ( $n = 436$ )



firms are subsequently divested. The acquiring company often sets the stage for eventual failure when it acquires companies in unrelated areas, fails to integrate the target properly, ignores negative effects of the merger on target employees that eventually erode productivity, and pays little attention to reestablishing leadership continuity within the target firm's top management team.

Not focusing sufficient attention on the issue of leadership continuity is especially critical. Instability within the top management team leads to the loss of firm-specific knowledge, damages established shareholder relationships, delays or terminates on-going strategic projects, and increases uncertainty over managerial discretion for executives who join the target several years after the initial acquisition.

Daimler-Benz's acquisition of Chrysler in 1998 for \$36 billion is one of numerous examples of acquisitions that fit this scenario. Many believed the acquisition of Chrysler was driven largely by the personal motives of Daimler-Benz's chief executive rather than synergy objectives. Performance deteriorated after the merger and DaimlerChrysler lost almost \$13 billion in market value through mid-2007, when it announced it would sell 80 percent of Chrysler to the private-equity firm Cerberus Capital Management LLC. The purchase price was \$7.4 billion.

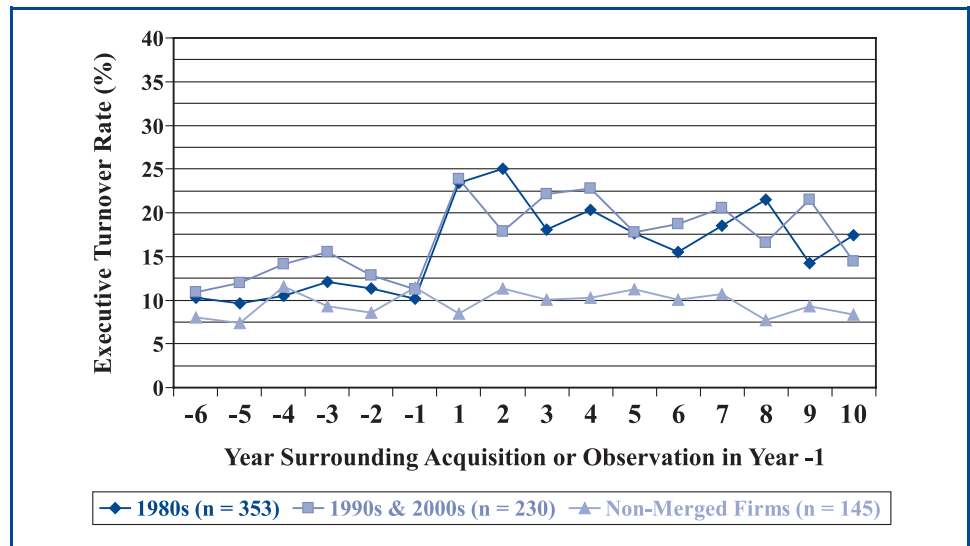
For Chrysler's executives and employees, the 1998 acquisition was followed by nine years of uncertainty, instability, and downward performance. Their acquisition in 2007 will undoubtedly lead to new rounds of restructuring, uncertainty, and changes in executive ranks as the new owners attempt to turn Chrysler around. One could point to other examples of acquisitions that have produced similar results for target firms. As we evaluate the acquisitions in the database in greater detail, it will be possible to offer greater insight into the causes of the instability experienced by these firms.

### Do high rates of executive turnover from M&As in the 1980s hold for M&As in the 1990s and early 2000s?

Figure 4 shows annual executive turnover rates for M&As completed in the 1980s, 1990s, and 2000s. Target firms acquired more than once during the study period were excluded. Acquisitions during the 1990s and early 2000s were combined to increase sample size and the validity of the statistical tests.

M&As have historically operated in cycles, with cycles showing common patterns. Unrelated acquisition activity, for example, characterized the merger wave during the 1960s. The M&A

**Figure 4** Top management turnover rates in M&As from the 1980s, 1990s, and 2000s



wave that began in the late 1970s and continued through the late 1980s was largely driven by related acquisitions. It also represented the first major wave of cross-border acquisitions, as European and Japanese firms made acquisitions in the United States, while USA and Japanese firms began investing heavily in Europe to take advantage of European integration.

The M&A wave that began in the 1990s has included much larger domestic and cross-border mergers. Many have been motivated to consolidate industry capacity, create scale advantages, and increase market power. Because different merger cycles often have different characteristics, it was important to determine whether the long-term leadership instability created by mergers in the 1980s also characterized more recent mergers.

*T*-tests indicate that, for the mergers completed in the 1980s, annual turnover rates were not significantly different between the target (10.7 percent) and non-merged firms (9.4 percent) during the six-year period leading up to the acquisition (target) or point-of-observation (non-merged firm) in year -1. For mergers completed in the 1990s and 2000s, however, turnover rates were significantly higher in the target firms during this pre-merger period (12.1 percent per year).

For the ten-year period following the acquisition, annual executive turnover rates were significantly higher for both groups compared to turnover in the non-merged firms. Mergers in the 1980s experienced an average annual turnover rate of 20 percent, while mergers in the 1990s and 2000s experienced an average executive turnover rate of 22 percent.

Two important conclusions can be drawn from these findings. First, mergers completed during the 1990s and 2000s produced patterns of long-term instability among the target firm's top management teams similar to those of mergers completed during the 1980s. Long-term instability appears to be a common result of M&As in general rather than a peculiar characteristic of mergers from the 1980s.

Second, mergers from the 1990s and 2000s experienced higher rates of turnover before the acquisition compared to the non-merged firms. Mergers from the 1980s did not experience higher pre-merger turnover rates compared to non-merged firms.

What explains the greater pre-merger instability of more recent mergers? Trends in competition, globalization, and technology during the last twenty years likely explain a great deal of this instability. Many USA firms in the steel, textile, automobile, semiconductor, computer, and motorcycle industries, among others, were subjected to intense foreign competition – predominately from Japanese firms – for the first time beginning in the late

**“Instability within the top management team leads to the loss of firm-specific knowledge, damages established shareholder relationships, delays or terminates on-going strategic projects, and increases uncertainty over managerial discretion for executives who join the target several years after the initial acquisition.”**

1970s and early 1980s. This led to a variety of import restrictions on foreign imports that were designed to give USA firms time to adjust to these new competitive pressures. Many USA firms shed unproductive assets, closed inefficient plants, thinned labor forces, and eliminated middle management layers during the 1980s and early 1990s to improve competitiveness.

During the 1990s, globalization trends intensified. While globalization presented many firms with an opportunity to leverage domestic capabilities and increase volume by selling in multiple countries, it also represented a significant threat to many firms. It subjected firms to competition from a greater number of firms located in a greater number of countries and to competition from a wider range of substitute products. Domestic firms also found that foreign consumers were less brand loyal than domestic consumers. Moreover, firms have increasingly had to negotiate prices with larger multinational suppliers with greater bargaining power.

Globalization has both stimulated and been driven by rapidly evolving technologies. Higher R&D and product development costs, for example, have forced firms to sell abroad to cover higher break-even points. In addition, shorter product life cycles have motivated many firms to integrate their worldwide value chains and standardize products and processes to lower costs. Deregulation and changing consumer preferences have further intensified competitive pressures and increased environmental effects.

In sum, globalization and technology trends have intensified competition and created greater industry turbulence for many firms. Greater instability among top management teams may be a natural consequence of these competitive and industry pressures.

### **Practical implications**

What do these findings mean in practical terms? First, we should expect high rates of executive turnover in the target firm shortly after the acquisition. We should also expect leadership instability to continue over the long-term unless action is taken to restore stability within the target's top management team. In accordance with our current state of knowledge of top management team effectiveness, we expect long-term instability in leadership to contribute to lower performance. Short-term turnover among executives immediately after the acquisition may be a natural and acceptable outcome of the merger event. Continued long-term leadership instability, however, should be viewed as potentially harmful to integration and long-term performance.

Second, globalization and technology trends should continue to intensify competition and increase environmental uncertainties for firms. This will put greater pressure on profitability and make strategy formulation more difficult. As a consequence, executives will be under greater pressure to be more actively engaged and will likely be held more accountable for performance outcomes. Thus, we should expect a certain amount of instability in executive leadership to continue given current trends and competitive pressures. The problem is to identify leadership instability when it occurs, understand the underlying causes and likely outcomes of this instability, and to take action to restore leadership stability in ways that increase decision making effectiveness and enhance long-term performance.

**Keywords:**

Acquisitions and mergers,  
Senior management,  
Leadership

There are a number of useful questions that we should ask. For example, was the firm acquired a few years before? Is the firm being divested? If so, is poor performance a cause? Was poor performance an outcome of poor integration by the acquirer, structure of the target's industry, or poor leadership in the target? What is the motivation for the acquisition? Is the target being acquired because of poor performance and leadership (i.e. market for corporate control) or is the acquirer interested in acquiring a valuable resource or capability? Last, what is the current state of stability within the target firm's top management team? Has it been relatively unstable compared to other firms? A history of leadership instability, poor firm performance, and industry turbulence within the target firm signals significant problems that will require greater effort and focus during the integration process.

### Note

1. In order to correct for the effect of multiple comparisons, Bonferri's method was used to adjust significance levels by multiplying the  $p$ -level by the number of contrasts (16). Contrasts that retained  $p$ -levels at 0.05 or above were considered significant.

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