

**Acquirers' prior related knowledge and post-acquisition integration: Evidences  
from four Chinese firms**

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# **Acquirers' prior related knowledge and post-acquisition integration:**

## **Evidences from four Chinese firms**

### **Abstract**

**Purpose** - This paper examines the role of acquirers' prior related knowledge in the post-acquisition integration process. The purpose of this study is to identify what constitutes the key prior related knowledge that can contribute to the reverse knowledge transfer following Chinese firms' outward M&As to Europe, and explain how prior related knowledge affects such transfer of knowledge.

**Design/methodology/approach** - The authors employ a multiple case study approach. Semi-structured interviews were conducted from February 2012 to June 2013 with 24 managers.

**Findings** - We find that, in addition to knowledge about the target, prior international business experience, R&D capability, and industrial capabilities are key components of acquirers' prior related knowledge that can contribute to the success of M&A integration and post-acquisition reverse knowledge transfer. Indeed, Chinese acquirers' prior related knowledge can influence the reverse knowledge transfer from acquired firms to acquirers by directly improving acquirers' absorptive capacity and building a harmonious organisational climate to facilitate such transfer.

**Originality/value** - This paper contributes to the absorptive capacity and the cross-border M&A literature. It extends our current knowledge on the key components of an acquirer's prior related knowledge in the outward M&A by Chinese firms. It also uncovers how post-acquisition reverse knowledge transfer is affected by acquirers' prior related knowledge.

**Keywords** M&A, prior related knowledge, absorptive capacity, post-acquisition integration, reverse knowledge transfer, Chinese firms.

**Paper type** Research paper

### **Introduction**

Mergers and acquisitions (M&A), as an important strategy for corporate growth and renewal (Cartwright and Schoenberg, 2006), have been studied for decades. However, the reasons for the high failure rate of M&A transactions are still poorly understood (Bauer and Matzler, 2013; Gomes et al., 2013). Recent M&A research has focused upon the process and socio-cultural factors to explain the outcome of M&A (e.g.,

Lupina-Wegener et al., 2011; Stahl et al., 2013; Sarala et al., 2014). This stream of research responds to the suggestion made by King et al. (2004) and Stahl and Voigt (2004), that more organisational and socio-cultural dimensions should be involved into a process perspective, and seeks to explain M&A performance in terms of the impact that key factors have on the post-acquisition integration process. These factors include national and corporate cultural differences (Stahl and Voigt, 2008; Teerikangas and Very, 2006; Sarala and Varra, 2010; Varra et al., 2012; Weber 1996), the levels of trust between the parties involved (Stahl et al., 2011; Stahl et al., 2012), the speed of integration (Angwin, 2004; Homburg and Bucerius, 2005), the post M&A leadership (Kavanagh and Ashkanasy, 2006; Nemanich and Keller, 2007), human resource management practices (Ahammad et al., 2012; Weber and Fried, 2011), the integration approach (Almor et al., 2009; Weber et al., 2009), knowledge transfer (Junni and Sarala, 2013; Sarala and Varra, 2010; Varra et al., 2012), and so on.

Despite these advances, important research gaps and paradoxes remain that leave many unresolved questions, such as the role played by culture, prior M&A knowledge/experience and pre- and post-acquisition linkage, and under-researched areas such as the roles played by power differences, integration speeds and levels of trust (Stahl et al., 2013). Among these research gaps, the role of prior related knowledge is relatively underexplored. Many studies consider prior knowledge as a key component of the firm's absorptive capacity (Cohen and Levinthal, 1990; Minbaeva et al., 2003; Minbaeva, 2007), and some recent M&A research has pointed to the importance of absorptive capacity in determining M&A performance

(Bjorkman et al., 2007; Deng, 2010; Junni and Sarala, 2013). Yet, our understanding of how prior related knowledge contributes to important post-acquisition integration process remains incomplete.

Specifically, the increasing number of firms from emerging economies buying firms in developed ones has drawn the attention of both the academia and practitioners (Birkinshawn et al., 2010). In this paper, based upon the experiences of four leading Chinese manufacturing firms, we aim at exploring the role of prior related knowledge in post-acquisition integration process following cross-border M&As. Chinese firms usually employ outward M&A to gain knowledge from their western targets which possess superior knowledge bases (Luo and Tung, 2007; Deng, 2009; Deng and Yang, 2015). It would be intriguing to examine how an acquirer's prior related knowledge could impact on gaining more knowledge from the acquired firms during post-M&A integration process through reverse knowledge transfer (Buckley et al., 2003; Rabbiosi and Santangelo, 2013). Our research questions therefore are: "What constitutes the key prior related knowledge that can contribute to the M&A success through post-acquisition reverse knowledge transfer? In addition, what else can prior related knowledge affect post-acquisition reverse knowledge transfer except the absorptive capacity of the acquiring firm?" Following mainstream M&A researchers such as King et al. (2004), we build our theoretical framework on Haspeslagh and Jemison's (1991)'s process perspective. This paper seeks to contribute to both M&A and absorptive capacity literature.

## **Literature review**

### *Knowledge transfer in M&A*

In this study, we define ‘knowledge transfer’ as the process through which a partner’s knowledge is successfully transmitted and beneficially utilised by the recipient. In the M&A context, knowledge transfer involves knowledge flowing in both or either directions: from the acquiring to the acquired firm and vice versa (Bresman et al., 1999; Junni and Sarala, 2013). The process perspective (Jemison and Sitkin, 1986; Haspeslagh and Jemison, 1991) suggests that the objective of M&A is to improve the competitive position of one or both parties by transferring knowledge and capabilities between them. This is in line with the knowledge based view (KBV) which argues that knowledge is a firm’s most significant resource, and that heterogeneous knowledge bases are the major determinants of a firm’s sustained competitive advantage (Kogut and Zander, 1992, 1993; Grant, 1996). The benefit inherent in being able to transfer knowledge across borders contributes to the competitive advantage of firms involved in cross-border M&A. Acquired firms in developed economies often possess superior knowledge bases; thus, Chinese firms usually employ outward M&A to gain knowledge and other forms of strategic assets from their targets (Luo and Tung, 2007; Deng, 2009). Accordingly, this study focuses on the reverse knowledge transfer from the acquired firms in Europe to the acquirers in China.

Extant literature has established that there is a clear connection between knowledge transfer and M&A success (Capron, 1999; Zollo and Singh, 2004). The proponents of the process perspective constantly argue that M&A’s value creation and

a firm's competitive advantage are achieved by means of the knowledge transfer between the combined units in the post-acquisition integration process (Bresman et al., 1999; Larsson and Finkelstein, 1999; Ranft and Lord, 2002; Westphal and Shaw, 2005; Reus, 2012). Their arguments emphasise the unification of the post-acquisition integration and value creation processes of M&A: while pre-acquisition factors such as the strategic, organisational, and cultural fits determine the synergy potential, the value of M&A is created in the post-acquisition integration phase because the extent to which that synergy potential is realised depends on the ability of the acquirer to effectively manage the integration process. Other research on knowledge transfer in the success of M&A examines how facilitators and obstructers impact on knowledge transfer (Bresman et al., 1999; Westphal and Shaw, 2005; Sarala and Vaara, 2010), and the characteristics of the knowledge transfer process actors, such as the absorptive capacity of the involved firms (Zaheer et al., 2010; Reus, 2012; Junni and Sarala, 2013). Indeed, absorptive capacity is considered as one of the most central determinant of knowledge transfer (Minbaeva et al., 2003; Minbaeva, 20007; Van Wijk et al., 2008). Recent M&A literature also suggests a positive relationship between the absorptive capacity of the recipient firm and post-acquisition knowledge transfer (Bjorkman et al., 2007; Junni and Sarala, 2013).

#### *Prior related knowledge and absorptive capacity in M&As*

Prior related knowledge is often regarded as the main antecedent of the acquiring firm's absorptive capacity. Previous research defined prior related knowledge as basic

skills, shared language, relevant prior experience, and up-to-date information on knowledge domains (Cohen and Levinthal, 1990; Szulanski et al., 2004; Minbaeva, 2007). It is an aggregation of the existing individual units of knowledge available within the organisation (Kim, 2001). In the context of Chinese firms' outward M&As to developed market, prior related knowledge was defined as knowledge of the target company, its market, and the host country (Deng, 2010). In this study, we follow mainstream absorptive capacity literature and define a firm's prior related knowledge as the combined abilities of its employees in terms of their personal knowledge base, such as individual skills, personal competencies and experiences. Firms need a certain level of prior related knowledge to understand, absorb and improve external technologies. According to Cohen and Levinthal (1990), a firm's absorptive capacity is mainly a "function of the firm's level of prior related knowledge" (p. 128). Although many studies in the related literature consider absorptive capacity to be on an equal standing with a firm's prior related knowledge, some recent research argues for a broader conceptualisation of absorptive capacity (Junni and Sarala, 2013). Minbaeva (2007) proposes that absorptive capacity includes both prior knowledge and the motivation of the organisational members, which affects the intensity of their effort to absorb knowledge from the partner. This argument is in line with Cohen and Levinthal's (1990) concept of absorptive capacity depending on the intensity of effort. Following this argument, Bjorkman et al. (2007) also define potential absorptive capacity as a combination of both motivation and ability on the receiving party to acquire capabilities from the other party. Considering that the main strategic intent of

most Chinese acquirers is acquiring resources and capabilities from the acquired firm (Deng, 2009; Zheng et al., 2014), the motivation for seeking and assimilating knowledge from the acquired firm through reverse knowledge transfer could hardly be lacking. Therefore, we consider the prior related knowledge of the acquiring firm as the main determinant of its absorptive capacity.

A few recent research provides insights into the prior related knowledge as an important component of a firm' absorptive capacity which determines M&A success. For example, based on a longitudinal quantitative study, Ahuja and Katila (2001) uncovered a positive relationship between acquired firm's existing knowledge base and the subsequent innovation output within technological acquisitions. In addition, Junni and Sarala (2013) find that employee withdrawal, which can lead to holes in the firm's overall knowledge base, reduces absorptive capacity both in the acquiring and acquired firms. Some recent studies on Chinese firms' outward M&A also shed light on this issue. Liu and Woywode (2013) argue that the integration approach of the Chinese firms' outward M&A in Germany is determined by the limited absorptive capacity of the acquiring firms. Building on a two-case comparative study, Deng (2010) argues that Chinese acquirers' high prior related knowledge of the target firm is an important component of their absorptive capacity, and can determine their ability to gain strategic assets through M&A.

These pioneering studies have identified the significance of Chinese firms' prior related knowledge on M&A success, and uncovered the absorptive capacity of the acquiring firm as the vital agent through which acquirer's prior related knowledge



impact on reverse knowledge transfer. However, important questions still remain: what constitutes the key prior related knowledge that can contribute to the M&A success through post-acquisition reverse knowledge transfer? In addition, what else can prior related knowledge affect post-acquisition reverse knowledge transfer except the absorptive capacity of the acquiring firm? This paper seeks to contribute to these important research gaps. A preliminary framework is developed, as is shown in Figure 1. This is based on the rationale in the current literature that an acquirer's prior related knowledge affects reverse knowledge transfer between firms through its impact on its own absorptive capacity. In the next section, we will explore what constitute this prior related knowledge and what else the acquirer's prior related knowledge can impact on to strengthen reverse knowledge transfer from the acquired firm in the Chinese firms' outward M&A in developed economies.

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### **Research methodology**

A multiple case study method is employed to explore this process-oriented and contextually-embedded research questions (Reddy, 2015). The case study method is suitable not only because of its strong aptitude for theory construction (Eisenhardt 1989), but also due to its highly preferable status when 'how' and 'why' questions are posed, when cross-culture and cross-border issues are involved, and when the

research concentrates on a contemporary real-life organisation (Flick 2009).

### *Case selection and data collection*

A theoretical sampling is used in this research, as it is generally deemed appropriate in research designed to build theory (Eisenhardt and Graebner 2007). With more than 100 billion USD worth of completed deals in the last two years, Chinese firms continued to be an important driver of international M&A around the world (Rhodium Group, 2015). Since 2012, the majority of Chinese firms have targeted developed economies to seek expansion through M&A, within which EU has experienced the largest increase in 2014 (Xinhua, 2014; Hanemann and Gao, 2015). Chinese firms' outward acquisition of European firms thus stands as an ideal setting for this research. As the core of China's economy, manufacturing industries underpin the drive of the internationalisation of Chinese firms through M&A (Deng, 2009). Therefore, cases chosen from the manufacturing sector can reduce any extraneous variation in the research (Eisenhardt, 1989; Schweizer, 2005)

Cases were chosen based on the following criteria: first, acquiring firms must have sought strategic resources and knowledge as one of the main motivations behind their M&A. Second, all cases must have completed their M&A deals at least one year before the first interview, so that sufficient time is allowed for the implementation of the post-acquisition integration (Angwin, 2004; Zollo and Meier, 2008). Third, we only chose the cases where acquiring firms' top executives can be approached, as they were the main architects of each company's post-acquisition integration strategy.

Following these criteria, we went through all the M&As conducted by the Chinese firms in the EU in the manufacturing sectors by reference to both public sources, such as various newspapers and websites, and restricted access sources, such as governmental authorities of several provinces in China. As a result, four firms were finally chosen. Table 1 shows a general description of each case.

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The primary data was collected through three rounds of semi-structured interviews from February 2012 to June 2013. In the first round, 19 face-to-face interviews were conducted at the acquiring companies' headquarters during two research trips to China. Five in-depth telephone interviews were then conducted with personnel of the acquired firms. After an initial data analysis, follow-on telephone interviews were carried out with several of the original interviewees to verify the original data and collect further information. Additional open-ended communication was also followed sporadically to contextualize and verify the data obtained from the formal interviews. The list of interview questions was derived from the research questions, with additional ones being asked to gather background and factual data. Back translation was adopted to ensure the accuracy of the translation of the interview questions (Brislin, 1970). In order to ensure internal consistency and to increase reliability, at least two top executives, including the CEO/president of each acquiring firm and the CEO of two of the acquired firms, were interviewed. Middle managers

directly responsible for the acquiring and acquired units, such as Secretary of General Manager's Office, were also chosen. The interviews were conducted in Chinese, and electronically recorded when permitted. Open-ended discussions were encouraged during the interviews. Secondary data, such as press releases, annual reports, TV interviews, and confidential internal reports, was also collected to provide multiple sources of evidence. It not only provided data with which the organisation and M&A background could be reconstructed, but also offered details on specific integration strategies and processes.

#### *Data analysis*

We relied on both deductive and inductive reasoning processes to interpret and structure the meanings from the interview data (Patriotta et al., 2013). The data analysis involved the following steps. We first cross-checked data from different sources for triangulation. This can help increase the validity and reliability of the research design, as well as to avoid any internal and external bias (Eisenhardt, 1989). We then started transcribing raw primary data. A comprehensive understanding of each case was developed around research questions through reading and open-coding all transcribed primary and secondary data. Third, we read and analysed data relating to individual cases based on the preliminary model, according to which the first order coding (such as knowledge, capability, R&D, knowledge transfer, past experience, learning, etc.) was structured. In line with the grounded theory research and inductive content analysis (Glaser and Strauss, 1967; Krippendorff, 2004; Patton, 2002), we

further specified the codes within the broad categories by including emergent codes and revising pre-defined codes. The analysis resulted in the identification of specified themes. Fourth, a comprehensive case report of each case was developed based on the identified patterns. Such within-case analysis was followed by cross-case analysis (Eisenhardt, 1989). Following a pattern matching logic, we iteratively sought patterns across cases by the cyclical reading and re-reading of empirical data and thus came to our findings with representative quotations drawn from the interview data provided to support the analysis. These quotations were translated by the second author before being back translated by a bilingual English native speaker to ensure consistency.

In order to increase inter-coder reliability, all data was analysed by both authors independently. Disagreements on coding were resolved by means of extensive discussions between the authors. This validation process was reiterated by continuously comparing findings with what is known in the current research.

## **Results and findings**

The results show that the acquirers' prior related knowledge not only provided the knowledge and capability foundation for the implementation of firms' integration activities, but also created an atmosphere that can support the reverse knowledge transfer from the acquired firms to the Chinese acquirers. In addition to knowledge about the target suggested by Deng (2010), the key components of the prior related knowledge that can contribute to the success of reverse knowledge transfer by the Chinese acquirers also include: prior international business experience, prior R&D

capability, and industrial capabilities.

*Prior international business experience*

Our data indicate that, with the exception of Case D, the case firms did not have past international M&A experience. Nevertheless, they accumulated useful knowledge and capabilities through their prior international exposure. These took the form of activities other than CBMA, such as running export/import businesses, setting up overseas offices and subsidiaries, building overseas factories, acquiring advanced equipment from global giants, collaborating with well-established corporations from developed economies and providing OEM business for global industrial leaders. A detailed comparative list of the prior international business experiences of the four acquiring firms can be found in Table 2.

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Their prior international business experience not only helped the Chinese acquirers in accumulating tangible resources and explicit knowledge-based resources, such as advanced equipment and technology, but also provided these domestic leaders with opportunities to build tacit knowledge-based resources in the process of dealing with cross-regional and cross-cultural issues. These knowledge and capabilities increased the knowledge base of the acquiring firms and greatly improved their ability to absorb strategic assets from the acquired ones (Deng, 2010). In other words, the

absorptive capacity of the acquiring firms was improved by their prior international business experiences.

In addition to the firm level absorptive capacity, that at individual level was also enhanced by operating advanced equipment, doing business or collaborating with foreigners and working in overseas subsidiaries. Although only a small proportion of the Chinese employees and executives directly involved in international business activities and benefited from these experiences, their improved absorptive capacity was clearly valuable for the Chinese acquirers in their management of the post-acquisition integration process. For example, in Case A, most of the middle managers involved in the acquisition had working experience in its international business subsidiary.

It is worth mentioning that, although prior international business experience was crucial in ensuring post-acquisition integration success, more prior international business experience did not always translate into better acquisition integration and performance. In fact, the most experienced firm, Firm D, showed the worst post-acquisition integration results. The reason was mainly two-fold. First, the timing of conducting outward M&A is vital for learning prior international business experiences. Conducting its acquisition in early 2004, Firm D was a pioneer in Chinese firms' internationalisation and outward M&A. At that time, Firm D could not learn lessons from other Chinese overseas acquirers. As the vice CEO of firm D commented:

*“In those years, Chinese acquirers did not have any idea on how to go about a real international acquisition...They (the acquired Western firms)*

*approached us and proposed acquisitions. Chinese acquirers, including TCL and Lenovo, knew nothing about how to acquire such giants. They (the executives of the acquired firms) taught us how to buy them (the acquired firms), to hire internationally renowned agencies, and to take every step... Our understanding of integration was very basic: we thought that, if we combined their technology with our diligence and low cost, synergies would automatically be achieved...We did not expect all those difficulties in the post-acquisition integration phase.”*

Similarly, the CEO of Firm D (Lanshizi, 2011) mentioned:

*“In the beginning (of the integration), we did not even know what our actual mistakes had been.”*

Conversely, the other three firms, which made their acquisitions seven years later, could easily learn direct lessons and experiences from those pioneers. These indirect experiences greatly helped latecomers to improve their knowledge base on the management of post-acquisition integration, and to form their own integration strategies. As the CFO of Firm C said,

*“You (the first author) may hear a lot about how Lenovo made great efforts and hit highs and lows during its integration with IBM. However, we were not like them. We chose not to go ahead with too much formal integration...”*

Likewise, both Firms A and B learned from the experiences of previous high-profile cases made by other Chinese acquirers. These lessons were directly related to Chinese firms or, more specifically, to manufacturing firms’ outward M&A in Western developed countries with the strategic intent to acquire strategic assets (Rui and Yip, 2008; Deng, 2007). Therefore, such experiences were valuable for subsequent Chinese acquirers to improve their methods for the management of post-acquisition integration process.

Second, the scale of M&A can affect learning of prior international business experiences. Although Firm D accumulated some experience in acquiring a Vietnamese manufacturing plant and partially acquiring a German electronics firm,



this was completely different from the whole acquisition of a global giant from a developed country. In addition, these past M&A experiences could even harm Chinese acquirers by instilling in them a false sense of confidence. By contrast to Firm D's overconfidence, the other three acquiring firms were more thorough and cautious when they undertook their acquisitions, and appreciated more the importance of post-acquisition integration. Most interviewees from both the executive and management levels of Firms A, B, and C clearly mentioned the vital stage of integration, and especially cultural integration, while informants from Firm D pointed out that they lacked understanding of post-acquisition integration:

*“It was totally different (from the experience before the acquisition of Thomson). We thought that there would not be too many difficulties...We simply used our Chinese logic (for solving any post-acquisition issues) and did not anticipate many potential problems. We did not expect things in France to be so different from China. After five years, we were still engaged in a lawsuit over labour issues”*

#### *Prior R&D capabilities*

One of the most significant embodiments of the Chinese acquirers' prior related resources was their R&D capability. As shown in Table 3, all four Chinese acquirers were industry leaders in their respective sectors and possessed top level R&D capabilities in the Chinese market, which provided most of these Chinese acquirers with sufficient ability to identify and understand the advanced technology and other knowledge-based resources of the target firms, so that they could assimilate and integrate these valuable resources within their existing knowledge and resource bases, transform them into combined resources and put them to commercial use (Deng,

2010). For example, acquiring firm A was the only firm in China that had sufficient R&D capability to assimilate the technology and products of the French target. One senior executive of Firm A stated:

*“Although there were other firms which could have afforded to acquire the French target, they would have found themselves in trouble afterwards, as they did not possess the capabilities necessary to assimilate the technology and carry on with the R&D.”*

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Insufficient prior R&D capabilities could hamper the realisation of any potential synergies out of M&A by constraining the transfer of knowledge from the acquired firm. This can have a particular impact on the transfer of explicit knowledge. Having an adequate level of prior R&D capabilities, an acquirer can gain explicit knowledge directly through documented patents and filed technology. The evidence shows that all four Chinese acquirers were able to absorb the technology, patents and standards of their acquired firms just by studying their files. As an executive of Firm A explained:

*“For example, we can learn their standards by studying their files. After some investigation, we can simply complement our previous files by adding some new elements learnt from our partner.”*

In other words, a sufficient level of prior R&D capabilities made the acquiring firms capable of absorbing explicit knowledge without the need for any direct coaching from the acquired firms. This provided the Chinese acquirers with an opportunity to adopt a low level of integration with their partners. As a senior management of Firm B stated:

*“We have almost obtained and assimilated all their core technology...”*

*without any direct coaching from the Italian engineers.”*

In fact, Firms A, B, and C allocated local managers with a high level of autonomy to make day-to-day operational management decisions so that executives from the acquiring firms just focused on transferring core technologies. Lower requirement in terms of the degree of post-acquisition integration can lessen the potential conflicts and value destruction brought about by key staff turnover, organisational routines disruption, etc., of a highly integrated acquired firm (Puranam et al., 2003; Puranam et al., 2006; Ranft and Lord, 2002). This can benefit the atmosphere in the combined organisation so as to foster the reverse knowledge transfer. Haspeslagh and Jemison (1991) suggest that creating an atmosphere that can support post-acquisition knowledge transfer is considered as the real challenge on top of the knowledge transfer itself, because post-acquisition integration is an interactive and gradual process in which individuals from the two organisations must learn to work together and cooperate to create value through knowledge transfer (Birkinshaw et al., 2000).

However, possessing national top level R&D capabilities may still be not enough for a Chinese acquirer to adequately manage its post-acquisition integration with an acquired firm from a developed Western economy. If the prior R&D capabilities of a Chinese firm were to prove not to be internationally compatible, it might still be confronted with difficulties in absorbing, combining and applying the acquired resources. For example, occupying a similarly leading position in R&D in the domestic industry, Firm D did not possess the same level of prior R&D capabilities by international standards as Firms A, B, and C did. Its R&D intensity was still relatively low compared to that of its global competitors. This was also in line with the global

status of China's economy and manufacturing ability at the time. As a result, Firm D could only passively accept the technology and patents from the acquired firm instead of exploiting and developing them. When those technologies fell into obsolescence due to new market trends, Firm D failed to use the acquired R&D resources to develop new technologies and products, which resulted in years of huge losses. In comparison, the R&D capabilities in the other three firms were not far behind those of their global competitors, even though they barely had any comparative technological advantages. Therefore, they successfully assimilated the acquired firms' advanced technologies on some key components and applied them to their existing main products.

#### *Prior industrial capabilities*

Following the definition of prior related knowledge in this study, the prior combined abilities of employees in an acquiring firm could incorporate industrial capabilities of the firm, such as its knowledge about the industry and ability of being competitive in the industry before the acquisition. For most Chinese acquirers, a high level of such knowledge and capabilities are normally associated with good performance and leading positions in the domestic market (Tan and Ai, 2010). This is mainly because, before any M&A, the overall capabilities and performance of a Chinese acquirer are examined by both the Chinese government (through a number of bureaucratic approval procedures) and the target firm. On the one hand, the Chinese government has set up a series of approval procedures to ensure the health of outward M&A

activities. On the other hand, a target firm would also wish to ensure a promising future for itself by selecting a powerful buyer.

A good prior industry related capabilities can help a Chinese acquirer to gain trust from the key stakeholders of their target firm, such as managers, local employees, trade union, and local government. The attitude of these stakeholders towards the acquiring firm plays a crucial role in the post-acquisition integration process, as the employees' trust in the acquired firm can lead to a high level of acceptance of the integration changes, keep intention to stay in the job and nurture willingness to cooperate with the Chinese executives (Stahl, et al., 2011). In other words, this trust is crucial for building an atmosphere that can support the reverse knowledge transfer in the combined entity. Therefore, *“it is important for us to make them aware of our past and current statuses, show our goodwill, and express our willingness to be responsible for the future of the firm.”* (Firm A, face to face interview with a senior manager, June 2012). In the studied cases, the trust and sense of security shown among the employees in the acquired firms largely originated from the strong performance of the acquiring firms in the Chinese domestic market. As one senior executive of Firm C recalled:

*“[After the acquisition,] there was a decline in the order volume [of the acquired firm], caused by uncertainty about the firm's prospect among many of its previous customers...the Spanish employees worried about the potential for decreased workloads and job losses”*

Nevertheless, job security among the foreign employees was greatly improved when executives of the acquiring Firm C revealed its money injection plan and promised not to cut salary and job opportunities even it received decreasing product orders.

These generous measures could hardly be adopted without the underpinning of the strong performance of the acquiring firms in the Chinese market.

Moreover, the trust can also be improved by the employees in the target firms to possess a positive perception of China and the Chinese economy. The employees of a target firm are more likely to believe that *“their firm could have a better future under the management of Chinese industry leaders”* (Firm C, face to face interview with vice CEO, June 2012), which have achieved dramatic economic growth and have sailed unscathed through the recent financial crisis. The evidence from cases A, B, and C proves that such trust and recognition were easily observed, which hugely helped the post-acquisition integration process. For example, when some Spanish employees were invited to visit the headquarter of Firm C, they voluntarily “attended the flag-raising ceremony with us. They also asked to wear our uniform and company badge” (Firm C, face to face interview with CEO, June 2012). It is worth noting that this effect was relatively weak in case D, which conducted outward R&D much earlier than the other firms, because the reputation of the Chinese economy and firms was still not well established at the time.

## **Conclusion**

This study has explored the role of prior related knowledge in the post-acquisition integration process of Chinese firms’ outward M&A to the EU. Using case study evidence, we find that acquirers’ prior international business experience, R&D capability, and industrial capabilities , are key components of an acquirer’s prior

related knowledge that can contribute to the success of post-acquisition integration process and M&A performance. We also argue that Chinese acquirers' prior related knowledge can influence the reverse knowledge transfer not only by directly improving acquirers' absorptive capacity, but also by building an atmosphere that can support such a knowledge transfer. A revised model of knowledge transfer in cross-border M&A is presented in Figure 2.

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This study contributes to the literature on absorptive capacity and M&A in several ways. First, it extends our current knowledge on the key components of an acquirer's prior related knowledge in the outward M&A by Chinese firms. Existing research on how acquisition experience affects M&A success shows mixed results (e.g., Gomes et al., 2013; Haleblan and Finkelstein, 1999; Hayward, 2002; Zollo and Singh, 2004). We find that Chinese acquirers can obtain prior related knowledge through learning from experiences of peer companies. In addition, possessing direct past international M&A experiences may even harm Chinese acquirers by instilling in them a false sense of confidence. This finding is in line with some recent research suggesting that acquirers with no prior M&A experience may achieve superior performance through learning from peers and the use of external consultants (DeLong and Deyoung, 2007). Moreover, previous research on Chinese firms' international M&A transpires that the key prior related knowledge of a Chinese acquirer is the

knowledge of the target firm, its market, and the host country (Deng, 2010). However, our research suggests that a general international experience represents useful knowledge, while a specific knowledge of the country where the target is located is not necessary to achieve M&A success. Understanding what knowledge needs to be possessed prior to the M&A is also managerially important. Managers of acquiring firms need to ensure that sufficient prior related knowledge is possessed before conducting any such M&A deals, and adopt suitable integration strategies based on the level of their prior related knowledge

Second, it contributes to the M&A literature by uncovering how post-acquisition knowledge transfer is affected by acquirers' prior related knowledge. Previous research has primarily focused on its impact on acquirer's absorptive capacity, while we find that it can also influence reverse knowledge transfer from the acquired firm to the acquirer by building an organisational atmosphere conducive to such knowledge transfer. International M&As are more difficult to manage compared with domestic ones due to the existence of national cultural differences, language problems and other institutional constraints. These obstacles can be contained through organisational atmosphere development, which can be achieved by accumulating adequate prior related knowledge. This argument is in line with the recent trend of a socio-cultural and human perspective of M&A, and similar to Bjorkman et al. (2007)'s proposal that cultural differences, which are another key factor of M&A success, can affect post-acquisition capability transfer through their impact on potential absorptive capacity and social integration of the two firms. Considering that prior related



knowledge already exists in the pre-acquisition stage, this finding also supports a recent argument for connecting pre- and post-acquisition stages to uncover M&A performance indicators (Bauer and Matzler, 2013; Gomes et al., 2013)

Although we claim this research to be a further step towards a better understanding of the role of acquirers' prior related knowledge in the post-acquisition knowledge transfer, it does present several limitations. First, the nature of qualitative studies limits the generalising ability of this research. Second, the present research is limited to Chinese manufacturing firms in European countries. Further studies could investigate across other industries and countries to provide a more comprehensive picture. Finally, given the relatively short history of Chinese acquirers' outward M&A, a quantitative evaluation of the prior related knowledge is very difficult at present. Future research should quantitatively test the finding of our research when more data is available.

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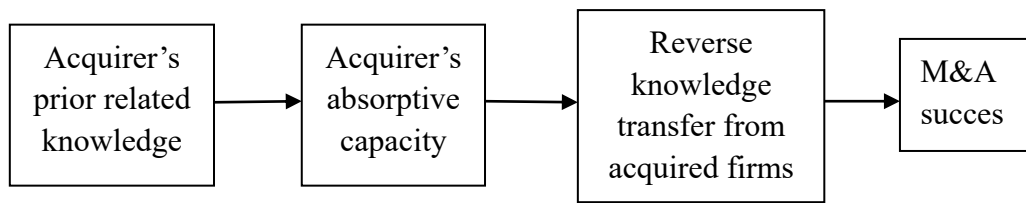


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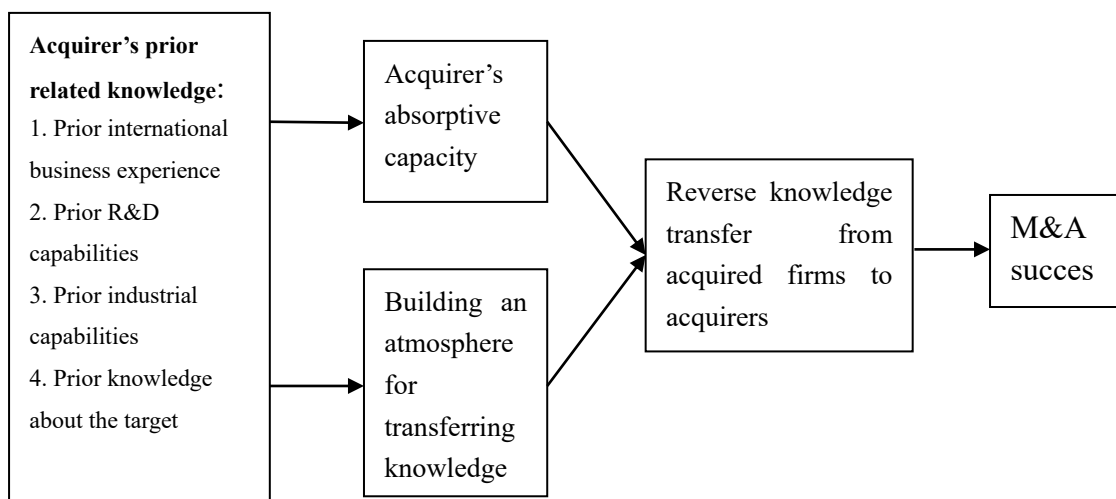
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**Figure 1.** Preliminary framework of knowledge transfer in cross-border M&A



**Figure 2.** Revised framework of knowledge transfer in cross-border M&A



**Table 1** Case selection criteria and variance of cases based on theoretical sampling

	Case A	Case B	Case C	Case D
Time of M&A	03/2011	02/2011	03/2011	01/2004
Core business	Agricultural and power machinery manufacturing	Heavy equipment manufacturing	Shock absorber manufacturing	Consumer electronics manufacturing
Status of the acquiring firm within the industry	First tractor manufacturer in China. Number one in market share.	One of the biggest players in the heavy equipment manufacturing industry; Number one mining machinery and cement equipment manufacturer	One of the biggest vehicle shock absorber producers in China. Number one in market share.	The biggest Consumer electronics company in China. Number one in the TV industry for years.
Motivation of M&A	Strategic intent. Seeking technology, market, and brand.	Strategic intent. Seeking technology, market, and geographical positioning.	Strategic intent. Seeking technology and market.	Strategic intent. Seeking technology, market, and brand.
Location of acquired firm	France	Spain	Italy	France
Ownership structure	SOE	SOE	Non-SOE	Non-SOE
Annual revenue before the M&A(CNY)	14.5 billion	0.544 billion	65 billion	25.4 billion

**Table 2** *Details of interviewees*

<b>Firm</b>	<b>Management level</b>	<b>Job titles of interviews</b>
<i>Firm A</i>	<b>Top management</b>	General manager; General manager (Acquired firm) <sup>a</sup> ; Chief technology officer (Acquired firm) <sup>a</sup> ; Secretary of the Board <sup>b</sup> .
	<b>Middle management</b>	Director of the General office; Anonymous (A department manager); Assistant to General manager <sup>b</sup> .
<i>Firm B</i>	<b>Top management</b>	General manager <sup>b</sup> ; Vice general manager; General manager (Acquired firm) <sup>a</sup> .
	<b>Middle management</b>	Anonymous; Secretary of the general manager; Anonymous (Acquired firm) <sup>a</sup> .
<i>Firm C</i>	<b>Top management</b>	General manager; Vice general manager; Anonymous.
	<b>Middle management</b>	Director of the General Office <sup>b</sup> ; Anonymous; International affairs secretary; The secretary of the general manager of the acquired firm.
<i>Firm D</i>	<b>Top management</b>	Vice CEO <sup>b</sup> ; Anonymous (Acquired firm).
	<b>Middle management</b>	Secretary of general office; Anonymous <sup>a</sup> .

<sup>a</sup>Interviewed through telephone calls in 2013.

<sup>b</sup>Interviewed again through telephone calls.

**Table 2** *The prior international business experiences of the Chinese acquirers.*

<b>Case</b>	<b>Prior international business experience</b>
<b>Case A</b>	Import and export; specialised international business subsidiary; overseas construction projects; ownership of overseas offices; spare parts centres and assembly factories.
<b>Case B</b>	Import and export; importing equipment from Germany; OEM business experiences for Western firms.
<b>Case C</b>	Setting up overseas offices and subsidiaries; import and export; overseas orders accounting for 10.79% of total orders
<b>Case D</b>	Import and export; setting up overseas offices and subsidiaries; overseas acquisition experience; international joint venture experience; partnerships with Western firms.

*Sources: Interview data, corporate documents and annual reports.*

**Table 3** *The prior R&D capabilities of the Chinese acquirers.*

<b>Case</b>	<b><i>Prior R&amp;D capabilities</i></b>
<b>Case A</b>	An R&D team of more than 2000 professionals and experts; a state-level technology R&D centre consisting of 11 advanced laboratories; ownership of the Chinese National Tractor Research Institute (CNTRI).
<b>Case B</b>	Annual R&D expenses over 5% of total sales revenues (a top level ratio); ownership of a shock absorber academic research centre with many specialists; including employees of the Chinese Academy of Engineering; 'National High-tech Enterprise'.
<b>Case C</b>	Being both a 'state level innovative enterprise' and a 'high-tech enterprise', it runs a national level enterprise-based technology centre (ranking among the top 10 of 887 such centres in China); runs a key state laboratory; runs a post-doctoral research station.
<b>Case D</b>	An innovation and technology oriented enterprise that had achieved many 'firsts' in China; one of China's innovative enterprises'.

*Sources: Interview data, corporate documents and annual reports.*