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Enhancing performance of cross-border mergers and acquisitions in developed markets: The role of business ties and technological innovation capability☆

Cong Cheng[a], Monica Yang[b,*]

[a] China Institute for SMEs, Zhejiang University of Technology, Liuhe road 288, Xihu district, Hangzhou 310023, China
[b] Willumstad School of Business, Adelphi University, Hagedorn Hall of Enterprise 329, 1 South Ave, Garden City, NY 11530, United States

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ABSTRACT

This study examines the determinants of performance of cross-border mergers and acquisitions (cross-border M & As) in developed markets initiated by firms from emerging markets. Drawing on social network theory and organizational innovation literature, we hypothesize that business ties of the acquiring firm increase performance of cross-border M & As via enhancing the acquiring firm's technological innovation capability and that environmental turbulence strengthens this mediating model. Moreover, the interplay of cultural distance and technological innovation capability would decrease performance of cross-border M & As. To test the model, we collected data from 186 Chinese firms initiating cross-border M & As in developed markets. As predicted, we found that (1) technological innovation capability of the acquiring firm positively mediates the relationship between business ties and performance of cross-border M & As; (2) environmental turbulence positively moderates the relationship between business ties and technological innovation capability; and (3) cultural distance negatively moderates the relationship between technological innovation capability and performance of cross-border M & As.

1. Introduction

When firms find themselves lacking needed resources in their home markets, they might consider acquiring resources overseas to remedy their resource scarcity. Recently, firms from emerging markets have been actively engaging in cross-border mergers and acquisitions (cross-border M & As) and one major motive behind these cross-border M & As is to seek strategic assets such as technologies, brands, distribution networks, R & D facilities and managerial competencies (Buckley et al., 2007; Deng, 2012; Kumar, Mudambi, & Gray, 2013). For example, Lenovo acquired IBM's personal computing division to obtain leading PC technologies, and Geely acquired Volvo to reach global markets beyond China. For acquiring firms from emerging markets, it is imperative to effectively transfer or integrate strategic assets from target firms and manage knowledge and innovation after completing these cross-border M & A deals. Nevertheless, some firms have enjoyed positive returns from cross-border M & As (e.g., Lenovo's acquisition of IBM's PC division or Geely's acquisition of Volvo) but some have failed (e.g., Shanghai Automotive Industry Corporation's acquisition of Ssangyong Motor, Ping An Insurance of China's acquisition of Fortis Investment). It is still not clear what affects the success of cross-border M & As aiming to acquire strategic assets of target firms in developed markets.

Social network theory argues that business ties are beneficial to firm performance (Burt, 1992; Granovetter, 1973; McFadyen, Semadeni, & Cannella, 2009; Zaheer & Bell, 2005). Business ties, defined as firms' networking activities with other firms, may help firms acquire both tangible resources such as raw materials or financial capital, and intangible resources such as knowledge and management practices (Athreye & Kapur, 2009; Cui & Jiang, 2010; Luo & Tung, 2007). Yet, it is not clear whether business ties of firms from emerging markets play such a role in contributing to the success of choosing and managing target firms located in developed markets. Moreover, business ties will not necessarily increase firm performance because it depends on *how* firms appropriately absorb and adapt external resources that business ties provide (Gao, Xu, & Yang, 2008; Wang, Jiang, Yuan, & Yi, 2013). For instance, previous studies in the network and organizational innovation literature (Ensign, Lin, Chreim, & Persaud, 2014; Li, Poppo, & Zhou, 2008; Peng & Luo, 2000) have acknowledged that the positive effect of business ties on firm innovation relies on other factors such as knowledge acquisition (Park & Choi, 2014),

☆ The order of authorship is listed alphabetically and both authors contribute equally.
* Corresponding author.
E-mail addresses: cheong@zjut.edu.cn (C. Cheng), yang2@adelphi.edu (M. Yang).

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technological innovation capability (Carlsson, 2006; Kafouros, Buckley, Sharp, & Wang, 2008) or absorptive capability (Gao et al., 2008). As latecomers to global competition, firms from emerging markets such as China are lagging behind firms from developed markets in their development of firm-specific advantages, especially in technology and experience in innovative activities and managerial capabilities (Luo & Tung, 2007; Wei, 2010). Therefore, it is questionable if the relationships among business ties, innovation mechanisms and firm performance supported by firms from developed markets are applicable to firms from emerging markets. For example, would technological innovation capability of acquiring firms from emerging markets fail to identify, adapt, and integrate information from their partners? Or would it play a significant role in mediating the link between business ties and performance of cross-border M & As? These interesting questions need further exploration so that our understanding of cross-border M & As by firms from emerging markets could significantly increase.

Drawing on social network theory (Burt, 1992; Granovetter, 1973; Uzzi, 1996) and the organizational innovation literature (Damanpour, 1991; Subramanian & Nilakanta, 1996), we propose a model that examines the relationships among business ties, technological innovation capability and performance of cross-border M & As initiated by firms from emerging markets in developed markets (see Fig. 1). We argue that business ties of the acquiring firm from emerging markets would positively influence performance of cross-border M & As via enhancing technological innovation capability of acquiring firm, a key mediator that captures the capability of the acquiring firm to adapt and undertake innovation (Carlsson, 2006; Kafouros et al., 2008). When acquiring firms from emerging markets receive information and benefits via their external ties with other firms, they would experience high acquisition performance when they exercise technological innovation capability to effectively manage information and strategic resources acquired. Furthermore, similar to firms from developed markets, acquiring firms from emerging markets are likely to actively absorb and exchange resources with their business partners when they face an environment with high uncertainty. Therefore, environmental turbulence serves as a contingent factor that fosters the relationship between business ties and technological innovation capability. Given that cross-border M & A activities involve cross-cultural issues, which would increase costs in communication and risks associated with liability of foreignness (Xu & Shenkar, 2002), we argue that the interplay of cultural distance and technological innovation capability would decrease performance of cross-border M & As.

To test the proposed model, we collected the data from 186 Chinese firms in the Yangtze River Delta Area initiating cross-border M & As in developed markets. The reasons why China was chosen are as follows. First, China is an active player in cross-border M & As, especially in acquiring strategic assets in developed markets (Chen & Young, 2010; Economist, 2013; Li, Li, & Shapiro, 2012). Second, Chinese culture values business ties and considers them as critical social capital, therefore, the social environment of China is appropriate to address our research question. A great deal of research has already demonstrated the importance of business ties to organizational growth and performance, especially in emerging economies such as China (Peng & Luo, 2000; Shu, Page, Gao, & Jiang, 2012; Wang et al., 2013). Finally, the Yangtze River Delta Area has been recognized as the center of China economy having the largest number of innovative firms active in outward foreign investment and acquisition, thus satisfying the requirements of our study.

This study contributes to the extant literature of social networks, organizational innovation and cross-border M & As in three important ways. First, by focusing on a cross-border setting, this study cultivates the understanding of *how*, and to what extent, business ties affect firm performance. Specifically, we present a key mediator, technological innovation capability of acquiring firms, to augment the ties-performance model. Secondly, this study extends the organizational innovation literature to a cross-border setting that acquiring firms from emerging markets enter into developed markets for the sake of strategic assets and resources. We illustrate that technological innovation capability of acquiring firms from emerging markets plays a critical role in facilitating business ties and affecting performance of cross-border M & As. Finally, this study contributes to the literature of cross-border M & As by identifying critical determinants for the success of cross-border M & As in developed markets by firms from emerging markets. Specifically, business ties and technological innovation capability of acquiring firms significantly increase performance of cross-border M & As, however, the strength of relationships of these three variables varies when environmental turbulence or cultural distance changes.

The rest of the paper is organized as follows. In the next section, we review the literature of business ties and cross-border M & A performance, followed by the hypotheses of the mediating and moderating relationships. In Section 3, we describe the data sources, variables and methodology used in this study. In Sections 4 and 5, we discuss results and future research directions. The final section concludes the paper.

2. Theoretical framework and hypotheses development

2.1. Business ties and performance of cross-border M & As

Business ties are defined as the extent of relational closeness between a firm and other relevant firms like suppliers, customers, and competitors in industry networks (Shu et al., 2012; Zhang & Li, 2008). Serving as a critical substitute for incomplete formal institutions, business ties provide a variety of advantages for firms such as obtaining customers (Peng & Luo, 2000), utilizing market opportunities and countering market threats (Carroll & Teo, 1996), building trust (Hoskisson, Eden, Lau, & Wright, 2000), obtaining business partners' support and overcoming institutional barriers (Kotabe, Jiang, & Murray, 2011; Li et al., 2008). In other words, building ties with business actors offers opportunities for accessing valuable knowledge and resources from these partners (Chen, Chang, & Lee, 2015). When a firm possesses more business ties, it receives more and various information from different firms. Moreover, "close" business ties facilitate information exchange, generate mutual trust and potentially provide information about competitors' actions (Cording, Christmann, & King, 2008). Thus, firms with strong business ties will have a better chance to improve their competitiveness and generate more new ideas/innovation (Pérez-Nordtvedt, Babakus, & Kedia, 2010; Uzzi, 1996). Those companies who possess strong business ties have often developed long and stable business relationships in supplying and marketing channels for products and services (Liu & Buck, 2007), resulting in increasing the speed of adapting to new changes. Nevertheless, the positive relationship between business ties and firm performance may not necessarily hold

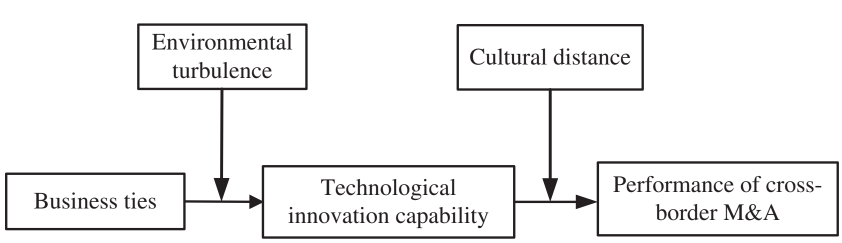

Fig. 1. The theoretical model of this paper.