ROLE OF COMMUNICATION AND HR INTEGRATION: A STUDY OF A BANK MERGER

A.Uday Bhaskar[1]
C.S.Venkata Ratnam
Kanika T. Bhal

ABSTRACT

Numerous studies in the literature have documented problems in post-merger integration and synergy realization. Some studies attribute mergers and acquisitions (M&A) failure to lack of concern for people issues while others blame lack of proper understanding of the situation by the acquiring managers. To enhance our understanding of the link between communication, HR integration, management action, and consequent contribution in post merger success, in-depth interviews were conducted in a recent merger of an Indian Bank. Based on the qualitative analysis, it was inferred that proactive communication, changes in organizational structure, and appropriate human resource (HR) systems integration would smoothen the journey towards successful integration.

INTRODUCTION

The phenomenon of change is all pervasive in organizations. One of the most radical types of organizational change is M&A, which have become common occurrence in the wake of competition and the ever increasing quest for growth and survival by organizations. There were over 30,000 M&As in the year 2004 alone and the value of these M&As is estimated at $1,900 billion, which exceeds the GDP of many large countries. There is at least one merger or an acquisition taking place every 18th minute (Cartwright and Schoenberg, 2006; Teerikangas and Very, 2006).

A merger is always associated with tremendous uncertainties and is a typical period of transition. Most of the M&A decisions are taken after examining the financial, legal and market related issues neglecting employees' concerns often leading to a great degree of employee uneasiness and stress (Johnson, 1989; Turner, 1996; Peters and Waterman, 1982). These anxieties and stress may arise partly because of the amount of secrecy, ambiguity and uncertainty surrounding the merger due to lack of adequate information to the employees. M&As also create a great deal of uncertainty for both employees of acquiring and target firms, which results in increased absenteeism, stress, lower productivity, health issues and commitment (Ivancevich et al., 1987; Schweiger & DeNisi, 1991). Many researchers (Hunt et al, 1987; Ravenscraft & Scherer, 1987; KMPG, 1997) indicate that about two-thirds of all mergers fail to achieve the desired results or outcomes, primarily because of the organizations' apathy to the employees' reactions and interests (Marks and Mirvis, 1982). Since anxieties, stress, ambiguity and uncertainty lead to psychological discomfort in an organization, work is likely to become a source of pain for the employee, resulting in reduced performance, efficiency, commitment, organizational citizenship behavior, and loss of trust in the immediate leader and the organization. Hence, there is a need to explore the human aspects of M&A.

HISTORY OF BANK MERGERS IN INDIA

M&A activity in the banking sphere increased in India after economic reforms in 1991. The main motive is to increase efficiency by reducing cost or increasing revenues or combination of both. Efficiency gains as a result of M&A were observed in the case of public sector banks in India (RBI Report, 2006-08). More recent research found economies of scale unexploited for larger banks as well in the US and in Europe and makes a case for banking M&A's.

It was found that M&A between distressed and strong banks in India showed persistent efficiency across time. Economic reforms have succeeded in weeding weaker/inefficient banks by merging them with healthier banks.

[1]Dr. A.Uday Bhaskar, International Management Institute, New Delhi. B-10, Qutab Institutional Area, Tara Crescent, New Delhi. India. Pin-110016. Dr.C.S.Venkata Ratnam, International Management Institute, New Delhi and Dr. KanikaT.Bhal , Department Of Management Studies, Indian Institute of Technology, New Delhi. E-mail: uday@imi.edu. Phone: 91-11-26529237/38.

TABLE: 1 POST REFORMS (AFTER 1991) BANK MERGERS IN INDIA

Sr. No.	Name of the Bank Merged	With whom Merged	Date of Merger
1.	Bank of Karad Ltd.	Bank of India	1993-1994
2.	Kashinath Seth Bank	State Bank of India	1st Jan 1996
3.	Punjab Coop Bank Ltd.	Oriental Bank of Commerce	8th Apr 1997
4.	Bari Doab Bank Ltd.	Oriental Bank of Commerce	8th Apr 1997
5.	Bareilly Corp Bank Ltd.	Bank of Baroda	3rd Jun 1999
6.	Sikkim Bank Ltd.	Union Bank of India	22nd Dec 1999
7.	Times Bank Ltd.	HDFC Ltd.	26th Feb 2000
8.	Benaras State Bank Ltd	Bank of Baroda	20th Jun 2002
9.	Nedungadi Bank Ltd.	Punjab National Bank	01.02.2003
10.	Bank of Madura	ICICI Bank	10th Mar 2001
11.	Global Trust Bank Ltd	Oriental Bank of Commerce	14th Aug 2004
12.	Centurion Bank Ltd	Bank of Punjab	1st Oct 2005
13.	CBOP	Lord Krishna Bank	29th Aug 2007
14.	CBOP	HDFC Bank	23rd May 2008

Source: RBI Report on Currency and Finance, 2006-2008

BACKGROUND LITERATURE: COMMUNICATION IN M&A

Communication, in terms of its quality and intensity, has been shown to be a significant factor in managing M&A effectively (Ivancevich et al., 1987). Management can deal with the individual employee reactions to the merger, and the anxiety and stress levels following a merger or acquisition through effectively and timely communication, informing all the anticipated effects of the change, associated with the merger. The aspects of communication are expected to focus on concerns to employees such as layoffs and changes in work rules, compensation, pensions, etc, (Ivancevich et al., 1987).

The kind of uncertainty that prevails during a merger creates stress for the employees and cannot be usually avoided as the ultimate outcomes are not known at the time of negotiations (Jemison & Sitkin, 1986; Schweiger & Weber, 1989; Schweiger, Ivancevich, & Power, 1987). Some studies have examined the issue, and inferred that communication might have decreased performance because of reduced uncertainty (Bastein, 1987), and increased communication in the form of employee-management meetings and even a merger newsletter have been shown to help (Napier, 1989).

During times of uncertainty and stress, people's attention to congruence and detail of communication is considerably heightened. So, when communication is not enough and incongruent, rumour mills develop to "fill in the blanks," lending worst-case meanings to acquiring company behavior (Marks, 1982, 1985, & 1986). The issue of secrecy in sharing information with the employees about the merger and the misrepresentation of the facts and figures about the merger are important dimensions of the communication construct. Providing realistic information will reduce unwanted uncertainty about the jobs, and rightly convey a message to the employees, that the organization they are entering cares about their needs and can be trusted (Dugoni and Ilgen, 1981; Meglino et al., 1988; Schein, 1985). The communication process which symbolizes an organization's concerns for its employees, elicits increased commitment (Schweiger and DeNisi, 1991).

Napier et al. (1989) has conducted a study in two merging banks. The main conclusions that came out of Napier et al. study are: 1) It seems that adequate communication is never there 2) Continuous and repeated communication from the top management is a necessity 3) The kind of communication has to depend on the hierarchy and it should vary depending on the level of employees. The findings of the Napier et al., (1989) is consistent with Ivancevich et al.'s (1987) that employees took much of the responsibility for managing stress and acquiring information. Research has found a link between success of an M&A to the quality of communication which has a positive impact on morale of employees (Brandon, 1999; Citera & Rentsch, 1993; Sloan, 1993. The unified message that stems from communication research in M&A is that to make a merger work, one should offer timely, full and open communication early in the process: the more the communication, the better it is for the organization. But who decides if the communication is enough? Who decides if it is timely, open, and full? While it seems to be good advice to communicate a lot, there are some problems.

HR INTEGRATION

The deal makers in M&A situations often ignore and downplay the significance of people issues in M&A (Harding & Rouse, 2007). When the employees' interests and concerns are not taken into consideration right from the planning stage of the merger, the merger might not yield the desired outcomes. Many researchers (Hunt et al, 1987; Ravenscraft & Scherer, 1987; KMPG, 1997) indicate that about two-thirds of all mergers fail to achieve the desired results or outcomes, primarily because of the organizations' apathy to the employees' reactions and interests (Marks and Mirvis, 1982).

There are a host of HR issues which affect the success of M&A like retention of key talent, work redistribution after lay-offs, salary and reward structure, redesigning of performance appraisal system, aligning the HR systems in the new merged entity, integration teams/committees, power balance between the two merger partners, etc. Loss of critical talent is considered a significant reason for M&A failure (Anon, 2000a,b). Lack of prior HR assessment, absence of sufficient communication push away key employees, out of the organization. Despite the best efforts of the acquiring management, some employees/managers always leave after an M&A. This adversely increases the workload on the remaining employees (Brockner, 1986; Gutknecht & Keys, 1993). A study conducted in the US in 50 M&A's found that 80% of the participating organizations have started downsizing and in 75% of the cases, work allocation was done by the remaining staff leading to work overload (Jacobs, 1988).

The harmonization of salary and reward structure has to be done. Management needs to take stock of the people who are crucial to the success of the deal. These key executives may be given stock options over an agreement. Some could also be given retention bonuses who stay with the merged entity till a certain time period (Schuler & Jackson, 2001). During the harmonization of the pay scales of the merged firms, some logic/rationale has to be given Ideally, the merged entity should have one grade structure, but this comes at a cost to the merged organization (Buddhwar et al 2007).

The organization structure for the merged entity has to be redesigned depending on the operating philosophy of the new entity (Ulrich, 2002). This is will help in integrating the two organizations through faster decision making, flexibility and better coordination. Employee appraisals systems need to be relooked and redesigned keeping in sync with the merger. This will bring uniformity in the assessments across the board and rewards can be linked with performance bringing transparency and acceptability in the system. The career development aspect of the employees during an M&A phase is very important. Many key employees leave the organization after M&A is announced because they feel/think that career progression might slow down as a result of the new management/policies. Appropriate career paths have to be designed for employees at all levels and they need to be communicated to get their commitment. Figure 1 presents the conceptual framework of the study.

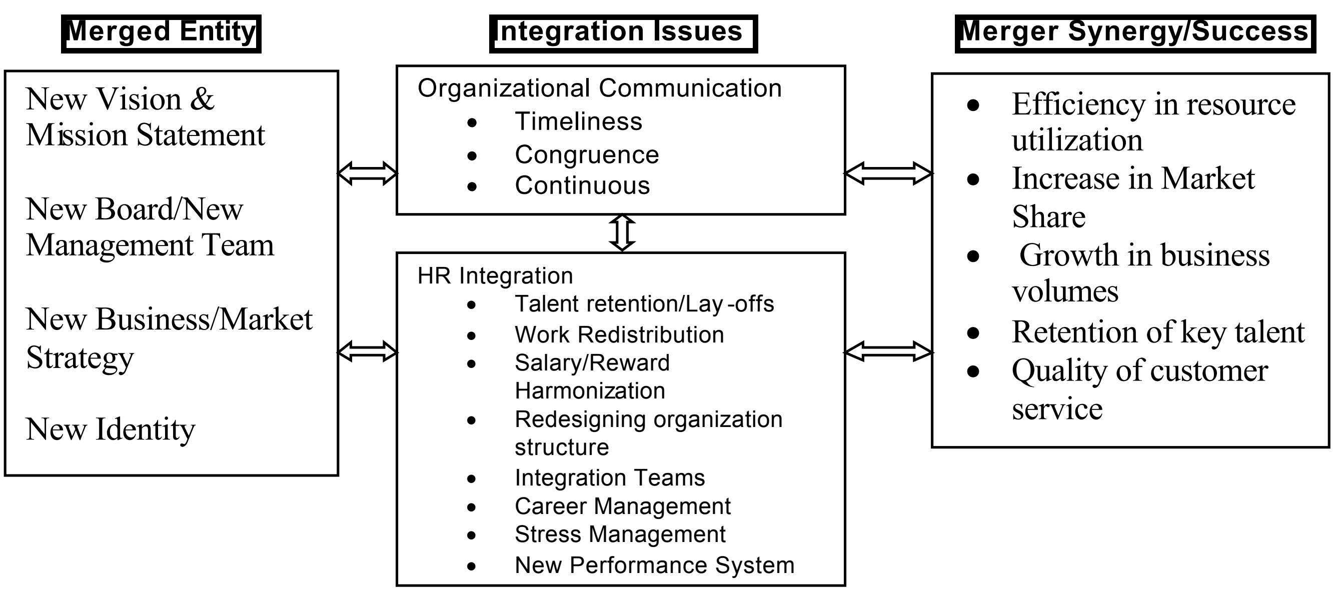

Figure 1: Conceptual Model of the Study

METHODOLOGY

This study was carried out in a merged private sector bank in India with branches operating in Northern and Western India with more than 2800 employees with a balance sheet size of 9, 3960 million. The merger took place 6 months before the interviews were conducted. Before the merger, both the banks had similar products and service offerings and were competitors of roughly the same size. Interviews were conducted with twenty managers of the merged entity. Six respondents were holding top management positions, eight were from the middle level management level and six were from the junior management level. Seven of the interview respondents were part of the joint integration team constituted for the merger integration process. The interviews were conducted during working hours. The interviews were semi-structured in nature. Extensive notes were taken during the interviews. Some interviews were recorded with the permission of the respondents. Only those employees were chosen for interviews who possessed a certain length of service with one of the merger partners to experience the merger in its entirety. Efforts were also made to ensure that the sample had an equal number of respondents from the two merging partners. All the respondents were males. The work experience of the employees ranged from a minimum of four years to a maximum of 19 years. Office memos, circulars, notifications (some of them confidential) were gathered with the cooperation and support of the employees. The identity of the respondents was kept confidential. The guidelines for the interviews consisted of open-ended questions that broadly fall in the four categories: communication pattern, changes in organizational structure, changes in operating style & HR systems integration.

COMMUNICATION IN THE MERGER

Interviews with employees of the two merging partners indicated that the communication of the merger was timely, continuous, accurate, and bi-directional. All employees said that they had been informed about the merger by their respective managements at least 12 hours before the news of the merger was flashed in the media. In fact, prior to the merger the managements of both banks had communicated to their respective employees their intention to merge the two banks. Both managements also clearly stated the rationale for the proposed merger. The first communication regarding the merger came via email from the managing director of one of the merger partners (hereafter referred to as CBL) and from the executive director of the other merger partner (hereafter referred to as BOP). The mails explained that the merger would improve revenues, increase market share, and enhance the brand image of the merged entity (hereafter referred to as CBOP).

A joint mail from the managing director of CBL and executive director of BOP assured the employees of both banks that ‘a detailed communication plan will be put in place so that everyone is kept informed of the next steps’. CBOP management made communication a two-way process by seeking employee inputs through a employee survey to elicit employee expectations and concerns. Mails were sent not only by top management but by the Merger Integration Team which was constituted to smoothen the integration process. Several ‘Town Halls’ were organized by the management at large cities like Delhi, Mumbai, Bangalore, Chennai, Ludhiana and Chandigarh. The idea was to address as many employees as possible. The chairman of the merged entity (CBOP) addressed the Town Halls in Delhi and Mumbai and managing director of CBOP addressed Town Halls in other places. The Town Halls provided the first opportunity for a consolidated interaction between the employees of both banks. The employees were told at the Town Hall meetings that there would not be any job losses nor people would be displaced through transfers. Interviews with the employees revealed that the promises were kept and there were no job losses and transfers. Employees, who sought transfer to their hometown, because the combined entity has more branches in different cities as compared to the earlier non merged scenario, were transferred to their home towns. The employees were also encouraged to post their queries, opinions and views to an e-mail address given to them. The idea was to address the concerns and queries raised via e-mails in the next Town Hall sessions. A set of employees frequently asked questions (FAQs) the context of the merger were posted to all employees by the HR Integration Team. There was also an FAQ guide for handling customer queries and concerns. Most of the mails sent to employees regarding the merger process were group mails. These mails were aimed at ensuring information symmetry. The mails tried to sensitize the people to the merger and asked them to be positive about the changed work environment in order to capitalize on the opportunities for growth opened by the merger.

CHANGES IN ORGANIZATION STRUCTURE

Prior to the merger, BOP had had a tall organization structure with thirteen levels, while CBL had had a comparatively flat structure with eight levels. The merged entity (CBOP) had eight levels. The structure of CBOP was rationalized and some levels like deputy vice president (DVP) of BOP were eliminated to align it with the CBL structure. All DVPs of BOP were promoted to vice presidents (VPs). CBOP and had different grades within a particular level. Career Level 5, which is senior manager level, had two grades (A and B). Career Level 7 (VP), had two grades (A and B) and Career Level 8 (senior VP), and had three grades (A, B and C). So, the DVP in BOP corresponded to Career Level 7 of CBOP. Since, there were two grades in Career Level 7 of CBOP, the DVPs of BOP were placed in Grade A of CBOP's Career Level 7. The grades in different career levels ensured uniformity in the organization structure post-merger.

Post-merger the organization structure of CBOP was streamlined. One BOP employee said, 'The nature of the job got streamlined because of the increased number of relationship managers and better distribution of work.' Now there were clear-cut divisions like Trade Finance, Cash Management Services, Credit, Consumer Banking, etc. Each division had a head, who had considerable power and autonomy to sanction resources to team members for good performance. The entire business model has changed post merger. The operations wing was separated from the marketing wing. A three-tier structure was created in the merged entity where one vertical looked after Non-banking products like Insurance, demat accounts and trading of securities, the second vertical looked at retail banking and the third was handling wholesale banking which including corporate banking and SME's.

A comparison of the organizational structures of BOP, CBL and CBOP reveals that the organization structure of CBOP was adopted from CBL (See Table 2). The employees of BOP benefited from this structure since all DVPs were elevated to the level of VPs since the CBL structure had no DVP level. Discussions with BOP employees revealed that the pay scales of BOP were lower compared to those prevailing in other banks. Promotion with or without a financial increment was considered a reward at BOP. That explains the number of hierarchical levels at BOP. In contrast, CBL salaries were competitive. CBL believed in faster and decentralized decision-making and therefore, had a flat structure. Hence the organization structure of the merged entity (CBOP) incorporated the strengths of both BOP and CBL.

Table 2: Organization Structure of the Merged Organization

Level	BOP Org. Structure	CBL Org. Structure	CBOP Structure (Merged Entity)
1	Front office executive	Junior officer	Career Level 1 A (Off)
2	Executive	Junior manager	Career Level 1 B (JM)
3	Assistant Manager	Assistant Manager	Career Level 2 (AM)
4	Deputy Manager	Deputy Manager	Career Level 3 (DM)
5	Deputy Manager	Manager	Career Level 4 (Mgr)
6	Deputy Manager	Assistant Vice President	Career Level 5 A (SM) Career Level 5 B (SM)
7	Manager	Vice President- 2 Level	Career Level 6 (AVP)
8	Assistant Vice President	Senior Vice President- 3 Level	Career Level 7 A (VP) Career Level 7 B (VP)
9	Deputy Vice President		Career Level 8 A (SVP) Career Level 8 B (SVP) Career Level 8 C (SVP)
10	Vice President		
11	Senior Vice President		
12	Junior Executive Vice President		
13	Executive Vice President		

THE MERGER PROCESS

Three leading consultants in different work areas were engaged to facilitate the bank with the integration process. They were:

1. KPMG Advisory Services Pvt Ltd: KPMG coordinated the activities of each of the functional teams in order to ensure integration of processes.

2. Mercer Human Resource Consulting: Mercer closely with the HR Integration and Management Teams of both the merging banks to understand the differences in people management practices at the two banks in order to design systems that would ensure meritocracy, transparency and fairness.

3. Wipro: Wipro managed the technology integration of BOP and CBL.

A cross-functional teams comprising BOP and CBL employees was constituted to focus on marketing, branding and public relations, keeping in view the brand equities of the two merging partners. The teams worked towards ensuring that the existing brand equity of the two partners was not diluted.

INTEGRATION PROCESS AND NEW MISSION STATEMENT

The functional teams identified the responsibilities for integration of their respective areas. All these functional teams identified the key integration priorities within their respective functional areas, and developed, designed and executed detailed work plans to integrate their functions. Each team had a team leader who was responsible for meeting the day-to-day targets. The individual teams reported to the HR Integration team, which in consultation with the functional specialists and senior management resolved issues and took decisions.

An Integration Kick-off Workshop was held in Mumbai for a representative set of team members. There were 16 joint integration committees that looked into the functions of the newly merged entity. Mercer sought feedback from the team members regarding the approach and process to be followed for the integration. Based on their response the consultant drew up a schedule for integration.

The mission statement for the merged entity was drafted. The members of the joint integration committee were made to chant the new mission statement in a chorus repeatedly.

HR ISSUES IN INTEGRATION

Retaining and rewarding talent was a top priority for the merged entity. CBOP was committed to the principles of meritocracy, transparency and fair play. The existing employment conditions and expectations were taken into account while determining the people management agenda for the merged entity. Post merger, the pre-merger terms of employment or contract pertaining to the grade, designation, location and compensation and benefits were adopted by the new entity. There was to be no discontinuity in the service tenure for the purpose of any provident fund, or other special scheme/fund/trust created by the BOP under which the employee was a beneficiary.

Reviewing Compensation Levels

The compensation levels of the two banks were reviewed in order to bridge any gaps. The aim of this review was to motivate, retain and reward talent equitably. Gaps were identified at some levels, and management had worked towards bridging these. The grades and HR policies for the newly merged bank were worked out and sent to all the employees within a month of the merger. There were marked differences between BOP and CBL compensation. CBOP was committed to offering its employees competitive compensation a combination of cash, performance based rewards like Variable bonus and Employee Stock Option Plans, etc. The HR team ensured timely dispatch of the compensation revision letters to BOP staff from the Corporate Office in Mumbai.

Performance Culture

CBOP wanted to create a culture of high performance and meritocracy. Prior to the merger CBL used to follow a performance-based reward structure. The focus was primarily on targets and numbers in terms of deposits generated, acquisition of new customers, new insurance policies taken and subscription to mutual funds. from th;e All items amenable to quantification were a part of the performance review yardstick. BOP on the other hand use to take a relatively softer stand as far as performance was concerned. According to Vice-President of BOP, 'in BOP with mediocre performance, we could grow. The culture in CBOP is of very high performance and one has to deliver outstanding performance to survive here, or else one has to quit.' The message was clear: one has to perform CBOP to survive. The performance rating of CBL was adopted at CBOP. The Key Result Areas (KRAs) were 75 per cent, which were hardcore and measurable, while 25 per cent was subjective, behavior, new contacts, networking, customer acquisition, etc. Above 'adequate' rated employees took a test for promotion. Even outstanding performers of BOP were classified as above average in CBOP.

Lay-offs & Work Redistribution

BOP had a large number of contractual employees at various levels, starting from sales personnel to officers on special duty (OSDs). A large number of these employees were in important positions like branch heads. The treatment accorded to them was at par with that given to regular employees. Some BOP employees felt that the HR policy at BOP was not sound in the sense that certain some important portfolios had been given to contractual staff.

Some contractual staff and a few regular employees who had crossed 60 years of age were asked to leave post-merger. The number of such exits was 78. The remaining contractual staff was to continue to work at CBOP till the expiry of their contract. The contract would not be renewed. CBL employees left the organization after the age of superannuation, but BOP employees continued in the organization on contractual basis. In cases of termination of contract three months' salary was paid in lieu of the notice period.

POST MERGER PERFORMANCE/OUTCOMES

Both the merger partners (BOP & CBL) were incurring losses individually. In the first year after the merger the merged entity earned profits of 800 million. Net profits for the fiscal year 2006-2007 were 1210 million. This represents a 38 per cent rise as compared to the previous year. Operating profit grew 144 per cent over the same period. The merged entity has reported the highest net interest margins in the industry at 4.6 per cent. The business volume has grown as well as the number of branches. Employee count has also increased by 50 per cent after the merger. The ranking of CBOP shot up three positions in the bank rankings. The NPAs were written off and the balance sheet was cleaned. The merged entity went on for a massive branch expansion. New managers were hired who has set up systems and processes and the work is now streamlined which added to the efficiency. Training programs were organized for all the employees on different areas of banking, finance, leadership, team work, computer training (finnacle training), etc. An idea generation scheme was introduced. The best ideas were rewarded a token amount of 50,000 INR. New incentive schemes were introduced. Incentives were as high as 40% of the compensation and fixed salary was between 55% to 60%. Both the banks were brought onto the same technology platform/banking software which increased operational efficiency. As a result of all these initiatives, the merged entity became No. 1 in Foreign Exchange Services and No. 3 in auto-loan business in the Indian banking sector.

DISCUSSION & SUMMARY

The research findings are based on a study of merger in the Indian banking sector. This sector is witnessing lot of M&A activity especially when banks are struggling on to hold up to the existing customers or acquiring new ones. The focus is also on economies of scale and efficiency gains. In the present case, communication was used as a strategic tool to address employee concerns/anxieties. The integration process was handled by professionals and by forming joint integration committees. A merger road map was created and HR integration was done as per that schedule. The study findings validate previous research in the area of communication and human factors in M&A. A unique feature of the merger is that hardly any full time employee of bank was asked to leave.

LIMITATIONS

The study findings are based on a single case study. Future researchers could take few more cases for better generalization of the findings. The data was collected through interviews with the employees which relied on participant recall which has its own limitations. Subsequent to the study, CBOP acquired Lord Krishna Bank. But CBOP itself was ultimately acquired by HDFC. The effects of these subsequent changes and resultant consolidation on people and competition require another study. Future research could gather data before and after the merger to know the real impact of M&A on performance of the merged entity.

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