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ACQUISITION TARGET SELECTION OF A SERIAL ACQUIRER

Case Kone Oyj

Master's Thesis
International Business

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1 INTRODUCTION

The introduction provides a background and purpose to the thesis. The background gives an insight to why the topic is chosen and some statistics of the history of mergers and acquisitions. The purpose describes more closely what the aim of this study is. The motivations to do this study, both personal and academic, are presented along with the limitations.

1.1 Background of the thesis

In the beginning of the twenty-first century the size of the 100 largest companies in any industry has become enormous. The reasons behind their size and power are acquisitions and mergers. (Lees 2003, 3.) The amount of acquisitions being made has risen constantly, but even larger growth has been in the size and value of the acquisitions (Angwin 2002, 33). Below there are statistics of global acquisition activity. The figure shows the amount of acquisitions made between 1999 and June 2010. It also shows the value of the acquisitions made. The acquisitions are divided in acquisitions made in the middle market, acquisitions that are undisclosed and acquisitions that are valued over \$750 million dollars.

Global M&A Activity

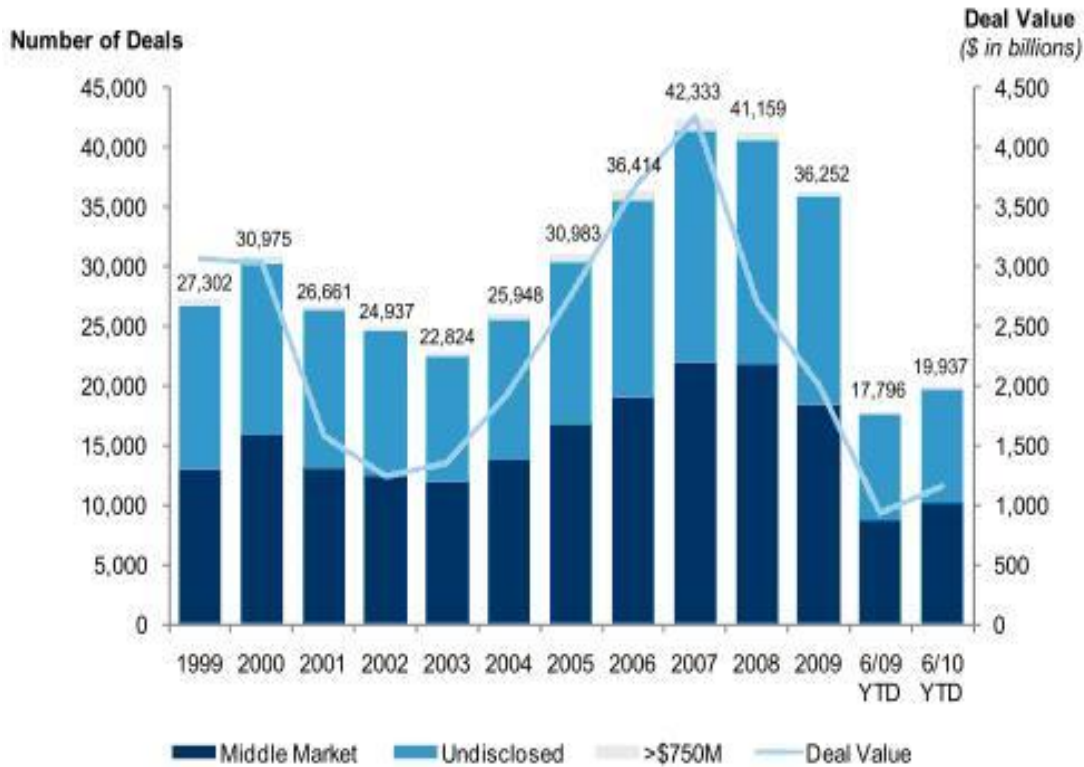


Figure 1 Global Acquisition Activity (PriceWaterhouseCoopers)

As can be seen in the figure above acquisitions made are substantial in size. In 2000 over 30 000 acquisitions were made and again in 2007 over 40 000 acquisitions. The total value of acquisitions made in the peak year of 2007 was close to \$4,500 billion. Even the amount of the acquisitions that exceeded the value of \$750 million was at its peak in 2007. The other observation that can be made from the figure is the way acquisitions occur in waves. Acquisition waves have been discussed comprehensively in literature (e.g. Gorton, Kahl & Rosen 2009; Rhodes-Kropf & Viswanathan 2004) but are left outside this study.

The peaks in acquisition activity in Europe during the recent years can be explained by macroeconomic, political and institutional factors. The nature of acquisitions is also changing due to hostile takeovers becoming a more common mechanism to improve the performance of inefficient companies. (Sudarsanam 2000, 120.) The acquisition waves are driven by globalization, technological change and deregulation. There is also a strategic mindset behind the acquisitions. Through acquiring new technologies, products and services, companies improve their current and future strategic positions in the domestic, regional and global market. Companies also increase their geographical pres-

ence and consolidate with competing markets by making acquisitions. (Schweiger & Goulet 2000, 61.)

There are many forces that drive takeover activity. Some of these forces are deregulation, synergies, economies of scale and scope, taxes, managerial incompetence, empire building and the increase of globalization. Other issues that contribute to acquisition activity are changes in technology or market conditions and the need for diversification, often at the expense of shareholders or the efficiency advantages when there is a need to exit an activity. (Jensen 1987, 427.)

Financial markets are also a driving power behind acquisitions and the restructuring strategies of an industry. The previous up-cycle period in markets once again reinforced acquisition waves. Reasons behind this were the availability of capital from private equity and hedge funds, new economies such as China and the Middle East and globalization. Motives for companies to acquire were pursuit of growth, scale and scope. (Smit & Moraitis 2010, 87)

There is a lot of literature about acquisitions and mergers (Miller 2007; Lees 2003; Angwin 2002; Buckley & Ghauri 2002), but most of the literature about acquisitions concentrates on the integration phase in acquisitions (e.g. Miller 2007), which takes place after the acquisition is made. There is also a significant amount of literature about acquisition failure and the reasons behind it (e.g. Gaughan 2005; Lees 2003). The literature that this thesis is mainly going to focus on is acquisition motives (Trautwein 1990). There is significantly less literature about acquisition motives and in general about the selection of companies to be acquired. Most of the research is also concentrating on the post acquisition phase of the acquisition rather than the pre acquisition phase. The post acquisition phase concentrates more on the integration of the acquired company whereas the pre acquisition phase is mainly about the selection of the target company and the preparation of the acquisition. In general acquisition studies concentrate on single acquisitions instead of serial acquirers. Based on these issues, there seems to be a research gap for a study about the pre-acquisition phase and more precisely about the process how acquired companies are selected from the point of view of a serial acquirer.

The focus in this thesis is also on serial acquirers and not only acquisitions in general. The previous focus in literature has been more on individual acquisitions and their performance (Laamanen & Keil 2008, 663). Therefore the two aspects, serial acquirers and acquisition motives, are discussed together in this thesis to bring a new insight to the subject.

1.2 Purpose of the thesis

The purpose of this thesis is to find out the reasons behind target company selection in the acquisition process of a serial acquirer. In literature companies that make several acquisitions a year are called serial acquirers or active acquirers. In this thesis serial acquirers are used as a synonym for frequently acquiring companies.

The focus is on motives and the linkage between acquisition strategy and other company strategies. The thesis is therefore studied from three perspectives: firstly the acquisition process is studied to find out the characteristics of a serial acquirer. Secondly the acquisition motives are studied through acquisition motive theories to discover whether the theories are compatible with the case company. Thirdly the relation between acquisition strategy and other company strategies is studied. Through this starting point the aim is to describe the acquisition process of a serial acquirer, to discover the reasons behind company selection, to study the acquisition motive theories and to see what the connection between acquisitions and other company strategies is.

This thesis will answer the following main research question:

- *What issues impact the selection of acquired companies from the point of view of a serial acquirer?*

The main research question will be answered by the assistant of the following sub-questions:

- *What is a buying process for a serial acquirer like?*
- *What are the motives for a serial acquirer to buy companies?*
- *What is the connection between company strategy and serial acquisitions?*

The research questions will be answered with the help of an interview made with Pekka Wikström, Vice President and Head of Alliances and Acquisitions at KONE. The findings concerning acquisition motives will be reflected on Trautwein's (1990) collection of theories about acquisition motives. In this study three of the seven acquisition motives will be studied. The acquisition strategy is analyzed along with competitive and corporate strategy.

1.3 Limitations of the research

The main limitation of this thesis is the use a single case approach and therefore the narrow ability to widely generalize the study to apply to other similar cases. Because the study is a one case study, it is also bound to the industry the case company operates in. The industry restrains the generalization of the results to other industries. Even if the study has its limitations, the aim is however not to generalize the findings. These limitations may though further more comprehensive studies about the subject.

The use of only three of seven of the acquisition motives gathered by Trautwein may also be seen as a limitation. For a more comprehensive study all of the theories could be studied in one case company or in multiple companies. In this way a wider perspective of the theories could be produced. The problem with some of the theories left outside this thesis is that they are very difficult to study. This is the reason why these theories were left outside this thesis.

2 ACQUISITIONS

This chapter defines acquisitions and how they can be categorized and describes the reasons behind acquisitions. A major aspect that is often brought up when discussing acquisitions is acquisition failure and therefore it is also brought up in this context. When a company makes several acquisitions each year, it can be categorized as a serial acquirer. There are some aspects that separate serial acquirers from companies that make occasional acquisitions. These serial acquirers are discussed more closely in this chapter.

2.1 Acquisitions in general

2.1.1 Reasons behind acquisitions

There are three major routes for a company to choose from if it desires to grow. These routes are growth through innovation, organic growth and growth through acquisitions. Acquisitions offer rapid growth and immediate access to the acquired companies markets and other assets. Through an acquisition a company may also improve operating efficiencies, diversify itself and rapidly grow in size and increase its market power. (Lees 2003, 3–4.) In an acquisition two companies of different qualities are combined.

A merger is a transaction where two or more companies come together and form a new company. In an acquisition or a takeover a stronger company acquires a weaker company. Acquired companies may be privately owned or they can be public companies. The nature of the acquisition in these two cases differs in the way that when acquiring a private company, the acquisition is very straightforward, but when acquiring a public company the shareholders of the acquired company are involved and the majority of the shares have to be acquired. A third type of acquisitions can also be recognized: a leveraged buyout. A leveraged buyout is made to achieve corporate restructuring and is made through a loan or venture capital finance to buy out a company's equity. (Morrison 2006, 406.)

The acquisition is usually a result of a mutual agreement, but sometimes the acquisition may be hostile. A merger happens when two equal companies are combined, but this is very rare. (Jagersma 2005, 14.) Mergers and acquisitions can also be distinguished in a way that in a merger two or more independent companies become one and in the contrary in an acquisition one company buys another company (Zettinig & Jokela 2002, 72). For a clearer definition, in this thesis mergers and acquisitions are referred as

acquisitions. In fact mergers are relatively rare; hence it is more appropriate to use the word acquisition.

There are different ways of categorizing acquisitions. Acquisition activity may be distinguished in five parts¹: horizontal, vertical, product extension, market extension and conglomerate². The four first types of acquisitions are made in related businesses. Conglomerate acquisitions are made in unrelated businesses and they have more financial characteristics. (Anderson, Havila & Salmi 2001, 577.) Acquisitions may also be distinguished in only three parts: vertical, horizontal and diversified. In a vertical acquisition a supplier or distributor is acquired, in a horizontal acquisition a competitor is acquired and in a diversified acquisition a company outside the industry is acquired. (Hodge & Anthony 1988, 219-220.) A horizontal acquisitions is also referred to as a consolidation and vertical acquisitions can be strategically valuable. Diversified acquisitions are usually made by large companies and it has been a way for them to grow. (Morrison 2006, 406.)

The main reasons for making acquisitions are the search for economic gains and diversifying the company (Anderson et al. 2001, 575). The other motives behind acquisitions may be divided in strategic motives, market motives, economic motives and personal motives. The strategic motives strengthen the companies' strategy by increasing its market power, improving its competence or creating synergy. Strategic reasons involve getting access to another company's products, resources or strengths. The main market motive in an international acquisition is to use the acquisitions as a method to enter new markets in another country. This is seen as the fastest way to enter a new market area. Establishing economies of scale and reducing costs through redundant resources are seen as economic motives for an acquisition and personal motives are related to the personal motives of managers which often do not align with the motives of owners. (Buckley & Ghauri 2002, 90-94.)

What a company desires through an acquisition is bigger size, risk reduction and efficiency, and through this it aims for higher profitability (Lees 2003, 33). Acquisitions are also seen as a normal activity in the different stages of business lifecycle. For example starting firms seek partners to help them grow or mature firms rather buy another firm with capabilities than develop the capabilities themselves. (Lees 2003, 4.) For a multinational company acquisitions are made because of the pursuit for strategic objectives. These kinds of objectives are the establishment of a position in a new market or the strengthening of the achieved position. (Meyer 2007, 43.) Even though acquisitions

¹ Following the U.S. Federal Trade Commission classification

² A large company formed by joining together different firms. (Oxford Advanced Learner's Dictionary of Current English)

have many benefits and for some companies it is normal activity in their business lifecycle, acquisitions are not uncomplicated and without the risk of failure.

2.1.2 Acquisition failure

In a research done on Forbes 500 executives, post acquisition factors are identified as contributing to acquisition failure. These factors are incompatible cultures, inability to manage the acquired company, unable to implement change, incompatible management styles and incompatible marketing systems. (Schweiger & Goulet 2000, 62.) Failure can also be seen in lower share value than expected, bad return on investment and low post-combination profitability. Some of the reasons behind unsuccessful acquisitions are acquiring the wrong company, overestimated prices, generally poor due diligence and misjudged timing. Often the problem lies in the entire process of making acquisitions. One specific reason behind unsuccessful acquisitions and the process of making them (selection of the target company, due diligence, price negotiations, integration etc.) can be pointed out. Many of the unsuccessful acquirers mainly focused on the financial data of the acquired company in the pre acquisition phase and this neglects the organizational and cultural differences, which play a significant role in the success of an acquisition. In contrary to unsuccessful acquirers, the successful acquirers focused in deals with a strategic mindset and an overall approach to the deal. (Marks & Mirvis 2001, 80- 81.)

Poor strategic rationale, insufficient financial evaluation of the acquisition, management of the acquiring company trying to reach acquisition premium, unsuccessful implementation of post acquisition integration and simply bad luck are yet more reasons behind acquisition failure. In many cases the source of the acquisition failure seems to be systematic. The failure starts in poor corporate governance and therefore insufficient monitoring of the stages in an acquisition process leads to failure. (Sudarsanam 2000, 120.) Failure can also occur due to poor cooperation or because the cost of cooperation exceeds the benefits of the efficiencies that are gained in an acquisition (Harrison, O'Neill & Hoskisson 2000).

Acquisition failure can be hard to define. When analyzing an acquisition failure from a simpler point of view, an acquisition has failed, if there has been a situation of over-paying. Some acquisitions are successful at one price, but failures at another. Then there are acquisitions that are not successful acquisitions at any price. So price is the deciding factor behind the definition of a successful or unsuccessful acquisition. (Gaughan 2005, 159; Harrison, O'Neill & Hoskisson 2000, 164.)

In a study, including foreign companies acquiring in the United States, it was recognized that acquisitions do not fail because of the lack of planning of the acquisition strategy by the acquirer, but because of the unsuccessful implementation of the strategy.

Three reasons behind acquisition strategy failure can be recognized: the financial costs were underestimated (i.e. financial costs are acquisitions costs, interest expenses and the total cumulative costs of competing successfully in the market for five to ten years), the strategic risk was underestimated (i.e. opportunities were lost in other geographical areas due to the efforts to get to the US market) and the acquirers overestimated abilities to implement the acquisition strategy. In this content with strategy implementation is meant the organizing of international operations, worldwide communication of strategies, production and market effort rationalization and the development of international management talent. (IMC Research Study 1990, 13.)

The overall reasons behind the unsuccessful acquisitions made by foreign companies to the United States were that the acquisition strategy of the acquirers did not correlate with their managerial and financial strengths. Neither did the acquirers competitive realities of the new market area correlate with their abilities. (IMC Research Study 1990, 13-15.)

2.1.3 Serial acquirers

The most common fields for serial acquirers have been in consolidating industries like telecom, banking and airlines. The acquisition strategy is usually based on a built-and-buy principle, where at the help of serial acquisitions a company acquires a platform in a sector and then with the help of this new platform expands its business geographically, product wise or acquiring more customers. This is not an easy way for a company to expand, but when successfully executed and in favorable circumstances the payout may be rewarding. The challenge a serial acquirer faces with having acquisitions as a part of its core business, is that it has to balance between the long term plans it has made for its acquisition strategy and the challenges, e.g. rival bids and market uncertainty that may change this plan. Sometimes the outcome may be very different from what the company has originally planned. (Smit & Moraitis 2010, 85- 86.) For a serial acquirer making acquisitions can be part of their core business. It can also be a strategy to grow. (Streeter 2007, 38.)

In addition to the short term advantages a company gains from making acquisitions, it can also create strategic advantages that can last for several years. These are long-term advantages that only multiple acquisitions can generate. Some of these advantages are routines and capabilities that help serial acquirers work with simultaneous and large number of acquisitions. Routines also reduce the time needed for each acquisition and make the acquisition processes more efficient. (Laamanen & Keil 2008, 663- 665.)

Size of the acquiring company affects the acquisition process and the larger the acquiring company is the easier it is to succeed in acquisitions because of managerial and

financial resources. In addition to size, a company's specialization in structures and processes involving acquisitions make the acquisition process easier. (Laamanen & Keil 2008, 665.)

According to Laamanen and Keil (2008) the acquisition frequency of a company affects its performance. The frequent acquisition rate generates positive outcomes that help a company make acquisitions more efficiently. In addition serial acquirers create acquisition programs over time that entails the optimal number and type of companies to acquire and when to acquire them.

2.2 Acquisition process

2.2.1 *Elements of the acquisition process*

The acquisition process of a company is all the phases containing the strategizing of the acquisition, forming a list of suitable companies to acquire, target selection, due diligence, negotiations, closing the deal and the integration of the two companies after the deal is closed in other words combining the companies. (Marks & Mirvis 2010; Schweiger & Goulet 2000.)

Integration of an acquisition is usually seen as a stage that takes place after the acquisition. The entire acquisition process can also be seen as integration. The integration begins from the target selection and is present all through the due diligence, negotiations, closing and even after closing the deal. In this way the success of the post acquisition integration process is determined as far ahead as from the beginning of the entire acquisition, i.e. from the first contact between the acquiring and the acquired company. (Schweiger & Goulet 2000, 65.) The stages of an acquisition can therefore be categorized as the pre combination phase, the combination phase and the post combination phase (Marks & Mirvis 2010, 27). The pre combination phase involves strategizing the acquisition, scouting for suitable candidates, assessing and selecting a company to acquire, making the deal and preparation of eventual combinations (Marks & Mirvis 2010, 53). The combination phase begins when the acquisition is legally approved (Marks & Mirvis 2010, 107). The last stage is the post combination phase that entails the integration of employees and other assets of the two companies (Marks & Mirvis 2010, 107).

In the pre acquisition process of the acquiring firm the company searches for suitable candidates for an acquisition. In the same process it also narrows down the list of candidates by rejecting companies that are not suitable for the acquisition. After the company has found a right amount of candidates, it increases its commitment towards one candidate it is willing to acquire. In a case of a related acquisition, strategy may increase the

probability of escalating commitment. The post acquisition process consists of different implementation styles. These are different steps the acquiring company makes to integrate the acquired company. (Harrison, O'Neill & Hoskisson 2000, 163.)

An acquisition process is generally divided in three phases: the pre acquisition phase, the moment where the deal is legally closed and the post acquisition phase. The pre acquisition phase and the post acquisition phase are much longer in duration than the closing of the deal, but the deal divides the acquisition process in two phases. Below is a figure that clarifies the process.

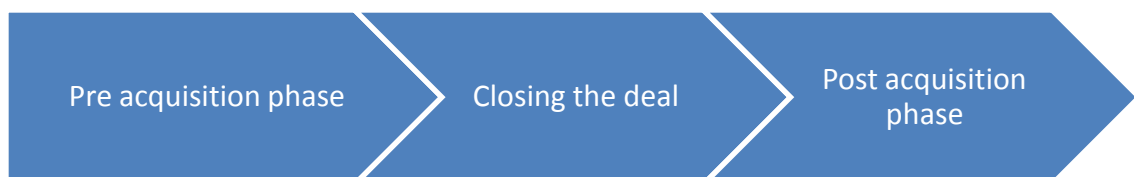


Figure 2 Acquisition process

The pre acquisition phase can also be called as the pre combination phase, the closing of the deal as the combination phase and the post acquisition phase as the post combination phase (Marks & Mirvis 2010, 27).

The duration of the acquisition process and more closely the speed of the integration are determined by the factor whether the acquisition is related or unrelated (i.e. in a related acquisition the acquirer buys a company that is in the same business and in a unrelated acquisition the target company is from a different business are). Related acquisitions need a high degree of integration in the later stage of the acquisition process, if the aim is to achieve synergy advantages. In unrelated acquisitions very little time to integrate the operations and resources of the two separate companies is needed. (Olie 1994, 385.) The speed of the acquisition process can also be a negative factor especially for a serial acquirer and affects the outcome of their acquisitions. The negative aspect in the speed is also the lack of learning of the previous acquisitions. (e.g. Hayward 2002.) Vuori (2012) discovered that the negative aspects of the speed of an acquisition can be softened through governing the target companies during the acquisition. The advantages are more substantial in partial acquisitions where there is left some ownership to the management of the acquired company. Other issues that reduce the negative aspects of a high acquisition pace are the size of the acquiring company being substantially larger

than the acquired company and the vast experience of making acquisitions of the acquiring company (e.g. Laamanen & Kiel 2008).

2.2.2 *A successful serial acquirer*

In general only about 25 percent of all acquisitions reach their targets and goals (Marks & Mirvis 2001, 80). Even though the statistics are unfavorable for successful acquisitions, there are companies that succeed with acquisitions time after time. The reasons behind their success are experienced deal teams. These teams have long term experience and get involved in all acquisitions from start to finish. This creates proactive opportunities and the teams create formal procedures for the acquisition process with clear guidelines. These guidelines are updated after each acquisition. The teams use walk-away-prices that are held on even to the very end of acquisition negotiations. This ensures the ability to walk away from a deal, if the deal does no longer seem sensible. They also have high-level approval and have a decision making process, where it is clear who recommends the deals and who makes the final decision about the acquisition. Other characteristics of a successful acquirer are making frequent acquisitions, not trying to time the acquisitions and acquiring significantly smaller companies in size compared to the acquirer. To become a successful serial acquirer a company should start with small, low risk acquisitions, build an organizational capability, institutionalize the process and learn from their mistakes through a feedback system (Cullinan, Rovit & Tymms 2003, 181-182).

Challenges in an acquisition can also be divided into strategic challenges and psychological challenges. Strategic challenges involve synergies that should be gained in an acquisition and a thorough due diligence of the acquired company to find the appropriate partner. Psychological challenges include the combination of two companies after an acquisition and the combining of the people in two different companies. (Marks & Mirvis 2001, 82-87.) Challenges can also be seen in the performance of an acquisition and success may be very hard to achieve. An acquisition aims often for synergy advantages, to create value and to preserve the created value. (Creating Value – (2011) 149-155.)

One factor stands out in companies that are involved in serial acquisitions. These are teams that are involved in the acquisition process. There seems to be a linkage between successful acquisition teams and successful acquirers. In a team that is responsible for acquisitions, the decision making role and responsibilities are clear. A design tool can be recognized: RAID. The combination of letter stand for: Recommend, Agree, Input and Decide. For example Nestlé is a company where these principles can be recognized. (Cullinan, Rovit & Tymms 2003, 183.) Below is a figure of the design tool that de-

scribes a successful acquisition process. The figure is modified from the word RAID to a circle, as it can be assumed that the process is ongoing for a serial acquirer.

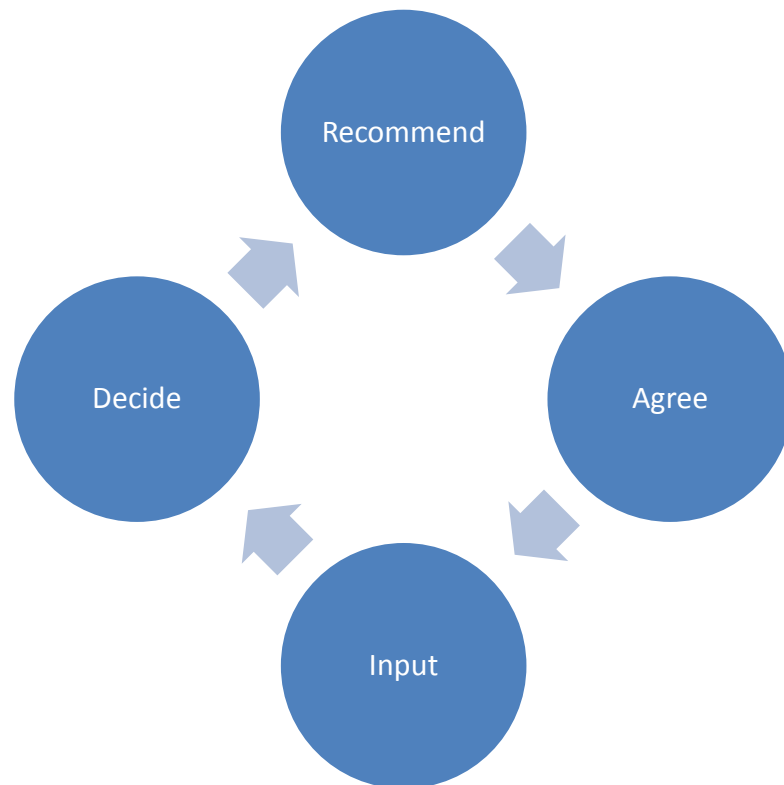


Figure 3 RAID

The four principles in the figure each represent a stage in a successful decision making process in a company making serial acquisitions. Only one person is responsible for the flow of decisions. *Recommend* means that the right parties may give their recommendations at the right time in the process. *Agree* means that the right people may agree on the course of the acquisition. *Input* stands for the contribution needed to make the decision and *Decide* is a principle that involves the right people making the final decision about the acquisition. (Cullinan, Rovit & Tymms 2003, 183.)

As Cullinan, Rovit & Tymms (2003) recognized, one of the reasons behind the success of some acquirers are successful acquisition teams. This is also recognized in the IMC Research Study (1990). The study pointed out that an acquisition team should be able to identify the best prospects of an acquisition, evaluate them correctly, negotiate terms efficiently and structure the acquisition successfully (IMC Research Study 1990, 29).

The acquisition process describes the stages of an acquisition and is more or less similar in different acquisitions. Nevertheless focus on the different stages in different acquisitions may vary. Whereas acquisition motives can be very different according to factors such as business area, company size or stage of internationalization.

2.3 Acquisition motives

2.3.1 Seven theories

There are different motives for a company to make acquisitions. Trautwein (1990) has distinguished seven theories of acquisition motives. These theories are efficiency theory, monopoly theory, valuation theory, empire-building theory, process theory, raider theory and disturbance theory. These theories focus on shareholder's interests, on manager's interests or on the deviation they have on maximizing shareholder value. (Trautwein 1990, 284.) The different acquisition theories are categorized more closely in the figure below.

Table 1 Theories of acquisition motives (adapted from Trautwein 1990, 284)

Acquisitions as rational choice	Acquisition benefits bidder's shareholders	Net gains through synergies	Efficiency theory
		Wealth transfers from customers	Monopoly theory
		Wealth transfers from target's shareholders	Raider theory
		Net gains through private information	Valuation theory
	Acquisition benefits managers		Empire-building theory
Acquisition as process outcome			Process theory
Acquisition as macroeconomic phenomenon			Disturbance theory

There are seven theories of acquisition motives as can be seen on the right hand side of the table above. According to the efficiency theory, net gains come through synergies

as in the valuation theory net gains come through private information. In the monopoly theory wealth transfers from customers, but in the raider theory wealth transfers from target's shareholders. Efficiency theory, monopoly theory, raider theory and valuation theory are theories that describe acquisitions as a rational choice. In the process theory acquisitions are seen as a process outcome and in the disturbance theory acquisitions are seen as a macroeconomic phenomenon. Empire- building theory states that acquisitions benefit managers as in efficiency theory, monopoly theory, raider theory and in valuation theory the acquisitions benefit bidder's shareholders. (Trautwein 1990, 284.)

This thesis focuses on three acquisition motive theories: efficiency theory, monopoly theory and valuation theory. The reasons for choosing these three theories are their clarity and plausibility. These theories also have characteristics, which can be studied in the case company. Characteristics of the other four theories are more difficult to study: empire- building theory focuses on managers own interest in an acquisition instead of shareholder's value. The personal interest of managers is a sensitive issue and the interest of managers to answer questions involving these issues can be assumed to be low. Process theory is a rudimentarily developed theory that sees strategic decisions about acquisitions as outcomes of processes instead of rational choices. These processes can be hard to define. In the raider theory some motives for making acquisitions relate to a financial compensation to the acquiring company from the acquired company after the acquisition and this is uncommon. Disturbance theory focuses more on acquisition waves and it stresses that acquisition waves are caused by economic disturbances. The study of the disturbance theory would need a different approach, because the analysis of acquisition waves through a single case study would not be comprehensive. (Trautwein 1990, 287- 290.)

2.3.2 *Efficiency theory*

According to the efficiency theory, acquisitions aim to achieve synergies by planning and executing acquisitions. Synergies can be categorized in financial synergies, operational synergies and managerial synergies. Financial synergies mean lower cost of capital and there are three ways of achieving these synergies: investing in unrelated business and in this way lowering the systematic risk of a company's investment portfolio, increasing the size of the company which leads to access of cheaper capital and by establishing an internal capital market. The benefit of an internal market is that it may operate on superior information which leads to more efficient allocation of capital. Operational synergies are achieved by combining operations or units that have previously been separate. These potential advantages and the cost of combining units of transferring assets have to be compared with the result to lead to profitable synergies. Manage-

rial synergies are realized when the acquired company's performance benefits of the acquiring company's managers superior planning and monitoring abilities. (Trautwein 1990, 284-285.) Synergy advantages are also achieved through costs savings from economies of scale and through successful combination of employees and assets in production and distribution (Jensen 1984, 114).

If an acquisition is made because of gaining synergy advantages, the managerial capability is a critical factor. The management's ability to integrate acquired companies is critical to success. The management's ability is in a key role especially in a case where the acquisition price is based on synergy values. (Schweiger & Goulet 2000.)

Synergy advantages can be found in financial savings, new resource combinations, revenue enhancements and in new knowledge. Financial savings can be achieved through consolidation, common sourcing and marketing, eliminating redundancies and economies of scale in contracts. New resource combination brings synergy advantages through, for example, grouping factories, sharing manufacturing and distribution and combining IT. Advantages by enhancing revenue are gaining through cross-selling, leveraging a larger customer base, or streamlining the supply chain and advantages in new knowledge are learning from each other's people, culture and distinct competencies. (Marks & Mirvis 2010, 11.)

2.3.3 *Monopoly and valuation theory*

In the monopoly theory acquisitions are planned and executed to get market power. Best gains through acquisitions are achieved by conglomerate acquisitions. The gains may be achieved through cross-subsidizing products; profits from one market are used to fight for market share in another market, through limiting competition in several markets; collusion with competitors and through deterring potential entrants from the market; making a concentric acquisition with a market leader. The advantage is wealth transfer from customers. (Trautwein 1990, 285-286.) It has also been pointed out, that advantages are not necessarily a monopoly market power itself created through acquisition, but the productive economies and synergies it produces (Jensen 1984, 114). The opposite can be recognized by Kulawczuk (2007) where an acquisition produced a monopoly environment and the market power allowed for example the acquirer to keep a certain level of pricing because of this position. There are also implications that the main acquisition motive in this acquisition would have been acquiring market power and the monopoly position in an environment.

Valuation theory argues that managers have better information about the target's value in an acquisition than the stock market or hidden interests in other companies and the acquired company is used only to gain ownership in other companies (E.g. Holderness

& Sheehan 1985, 576). The theory claims that managers have unique information about the advantages of a possible acquisition or that managers have detected an undervalued company. The ambiguity of the private information makes it hard to value the advantages it entails. Through private information net gains can be achieved in an acquisition. (Trautwein 1990, 286- 287.) These net gains can be achieved, when inside information gives a company more value than the market has valued it to have. Even efficient markets cannot draw a picture of a company's true value if one buyer possesses inside information. (Jensen 1984, 113.)

Even though the theories presented above may be justified, they are not without critique. As many theories they can be criticized with counter evidence.

2.3.4 *Theory critique*

All of the theories have been criticized. Below there are the three theories used in this thesis. For clarification they are separated from the original figure. On the right side of the figure there are the theories and on the left side motives behind these theories.

Table 2 Three acquisition motives (Trautwein 1990, 184)

Net gains through synergies	Efficiency theory
Wealth transfer from customers	Monopoly theory
Net gains through private information	Valuation theory

The efficiency theory has been criticized because it is argued that financial synergies cannot be achieved in an efficient capital market and neither can the systematic risk be lowered (Montgomery & Singh 1984, 189). The study made by Montgomery and Singh 1984, was conducted with a small sample of unrelated companies and the results can therefore vaguely be generalized, as they themselves recognize. The monopoly theory has received even more critique because acquisition announcements in a monopoly situation do not give clear messages in the stock market (Jensen 1984, 114). Private information is the main motive in the valuation theory and the theory is criticized because private information is seen to be ambiguous and not one-dimensional. The reaction to private information should also cause a different reaction in the stock market. (Wensley 1982, 148.)

When studying acquisitions, they have to be seen as a part of the company and its operations. Therefore it is justified to study the linkage between acquisitions and company strategy.

2.4 Company and acquisition strategy

2.4.1 *Competitive strategy*

There are two levels of strategy in a company: the competitive strategy and the corporate strategy. The competitive strategy focuses on creating competitive advantage in all the businesses a company competes in. (Porter 1987, 43.) Competition is also a factor that determines the success or failure of a company. The core of competitive strategy is finding the favorable competitive position in the industry. Through this position a company can defend itself against industry competition. The choice of the competitive strategy depends on the attractiveness of the industry regarding long term profitability and the relative competitive position inside the industry. There are other factors too that determine the competitive strategy of a company and both the attractiveness of an industry and the competitive position within the same industry are factors that change over time. In an industry, a company may affect the attractiveness and the competitive position by its own choice of competitive strategy. (Porter 1985, 1-2.)

A company has to choose from two competitive strategy approaches according to the position in the industry and its competitors. To have an effective strategy it has to choose from an offensive or defensive strategy. These strategies create a defensible position against the competitive forces of an industry. (Porter 1980, 29.) The competitive forces are: threat of new entrants, rivalry among existing companies, threat of substitute products or services, bargaining power of suppliers and bargaining power of buyers (Porter 1980, 4).

There are differences in the competitive strategies of acquirers, the effectiveness of their operations and how they perform in their acquisitions. Acquirers that effectively carry out their operations gain greater performance improvements in acquisitions they make. The acquisition performance is also higher with companies that have a broad competitive strategy. In contrast mixed competitive strategies affect negatively the acquisition performance. A mixed competitive strategy would be a strategy combining cost leadership and differentiation. (Mudde & Brush 2004, 75.)

2.4.2 Corporate strategy

The corporate strategy focuses on the questions concerning the type of business a company should be involved in and how the corporate office should manage the array of business units. Corporate strategy is the element of a company that brings added value that is more than only the business units it has. A good corporate strategy adds value to the company. (Porter 1987, 43-46.) Acquisitions can also be seen as a popular corporate strategy (Harrison, O'Neill & Hoskisson 2000, 158).

Corporate strategy has had different aims. It was previously seen as a tool to achieve synergy advantages and decentralize the business units. Now portfolio management is seen to be the main task of corporate strategy. (Porter 1985, 318.) The corporate strategy of a company should not be a choice that is done only once, but it should evolve according to the vision a company has.

Corporate strategy is also used to create shareholder value. This value is achieved when the corporate strategy shifts from portfolio management towards sharing activities. The corporate strategies that bring shareholder value can also be more closely be recognized in four ways: defining the company's role and objectives, having the right skills to fulfill the concept's conditions, organize the company to manage the diversity of the company in a way that is compatible with the strategy and be in the right capital market environment. (Porter 1987, 57.)

The corporate strategy a company has chosen is partly a legacy of its past. This can well be recognized in the corporate strategy and more closely in the acquisition strategy of the case company of this study. A company's corporate strategy is also successful only if the company's role and objectives are clear, the company has the right skills to manage the strategy, the ability to organize itself and the company is in a right capital market environment. Because of these reasons, the portfolio management approach to corporate strategy is valid only in certain circumstances. (Porter 1987, 57.)

2.4.3 Acquisition strategy

Acquisitions can be for a company a strategy to grow. The growth can be natural or it can be forced. There are situations where a company is forced to make acquisitions to survive and at the same time it grows through these same acquisitions. These forced acquisitions are made in a situation where a company has to "eat or be eaten". These kinds of situations are also called as the "Pac-Man defense" where the principle is: "My company will eat yours before yours eats mine". In this kind of situation the focus is not on the question whether one of the companies will be acquired, but on the outcome and which manager will be the one in control after the acquisition. (Jensen 1984, 110).

For some companies it is also challenging to grow organically. Acquisitions are a way to build scale and add new competencies. Investor expectations are hard to meet and therefore acquisitions, if done correctly, are a way to meet their targets. (Cullinan, Rovit & Tymms 2003, 182.)

The acquisition strategy can be divided according to the characteristic of the companies that are acquired. Strategies can involve acquiring related or unrelated companies. In related acquisitions the acquiring firm does not have to change much of its processes. The advantages of related acquisitions are managerial skill transfer, ability to use common marketing channels, research methods, advertising media and suppliers. In an unrelated acquisition the acquiring firm is not expected to understand the business of the acquired company, because the acquirer does not have a thorough understanding of the business the acquired company operates in. Target resistance is also an issue that arises often in unrelated acquisitions. (Harrison, O'Neill & Hoskisson 2000, 167.)

The figure below demonstrates one possibility of an acquisition strategy. The figure is modified from a US acquisition strategy presented in the IMC Research Study (1990). The corporate mission statement has to be approved by the board of directors. After this the strategy statement is prepared by the CEO and senior management. The statement is based on global situation analysis, analysis of the company's strengths and weaknesses and the analysis of the company's competitors. (IMC Research Report 1990, 18).

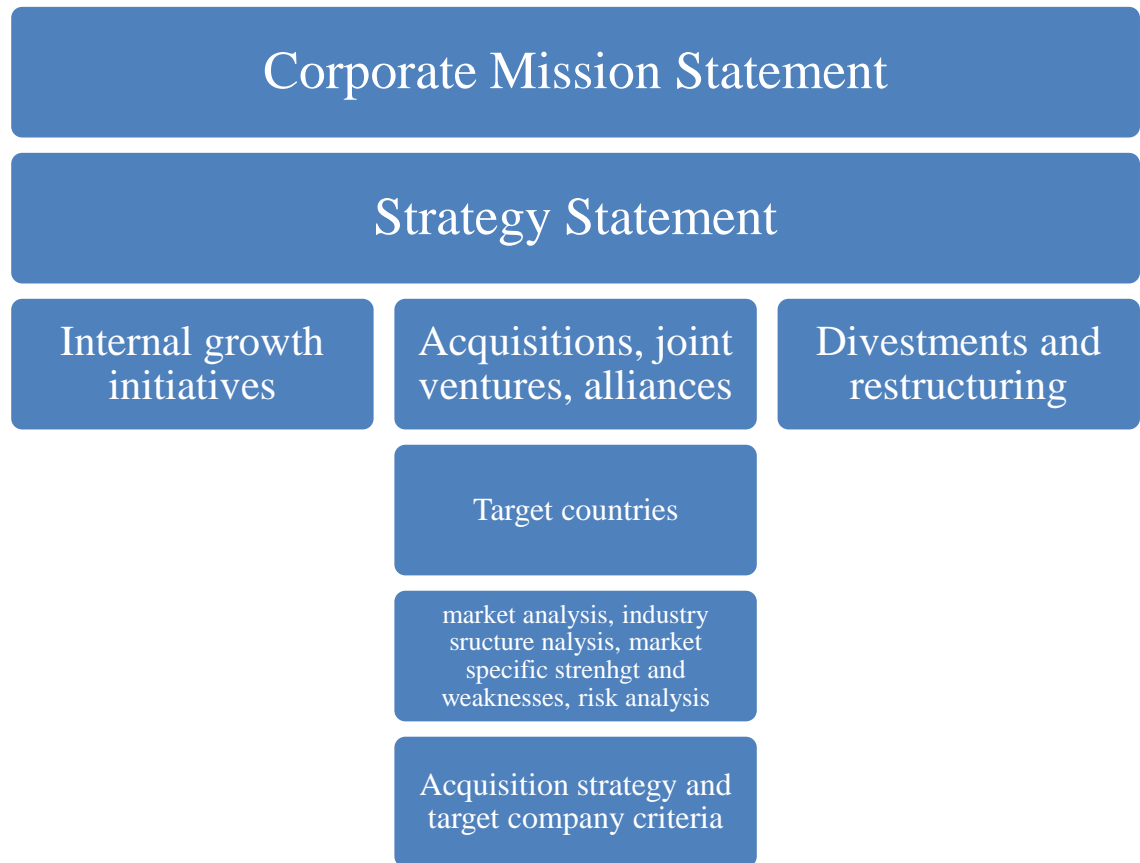


Figure 4 Acquisition Strategy (modified from IMC research study 1990, 19)

The strategy of the company is divided into three parts: the initiatives for internal growth in the company, acquisitions, joint ventures and alliances and divestments and the restructuring of the company. Acquisitions, joint ventures and alliances are then divided according to the country they are made in. They can be made both in the domestic market and foreign countries. Before the acquisition strategy is complete, the target market, the industry structure, the strengths and weaknesses of the market and the risk have to be analyzed. After this a company has an acquisition strategy and the criteria for the target company it desires to acquire. The development of the strategy requires investigating industry surveys, situation audits, analyses about strengths and weaknesses in the specific market area. These all involve strategic, managerial and financial input by the CEO and his team. (IMC Research Study 1990, 18-19.)

In the contrary to the findings of the study presented above (IMC Research Study 1990), Vuori (2012) points out that the setting where the acquisition is made and the characteristics of the acquisition is not the only determining factor of the acquisition strategy. In her study different companies acquiring in the same setting used different strategies. The differences in their strategies were based on the cultural differences between the acquiring company's home country and the country of the target company and information asymmetry. The different strategies, or approaches, that acquiring companies used in the same settings, meaning in the same industry and the same country, were different in the sizes the companies acquired in the target company (i.e. varying from partial to full acquisition), had different policy to replace top management (i.e. keeping the managers of the acquired company or replacing them with managers from the acquiring company), had different partners (i.e. some had large local companies as partners, when others cooperated with local authority) and the pace and rhythm of the acquisitions were different. (Vuori 2012, 88-89.)

2.5 Acquisition synthesis

The acquisitions and the acquisition target selection are divided in this thesis in three aspects: the acquisition process, the acquisition motives and the linkage between company strategy and acquisition strategy. Below is a figure that summarizes the three aspects and the theories.

Acquisitions	Process	Pre acquisition, making the deal, post acquisition
	Motives	Efficiency theory, Valuation theory, Monopoly theory
	Strategy	Linkage between company strategy and acquisition strategy

Figure 5 Acquisition synthesis

Acquisitions are in this thesis divided into the acquisition process, the motives behind making acquisitions and the linkage between company strategy and acquisitions strategy. The acquisition process may be divided into the pre acquisition phase, the deal making phase and the post acquisition phase. This thesis focuses mainly on the pre acquisition phase. The pre acquisition phase is used as a synonym for the pre combination phase and it involves strategizing the acquisition, scouting for suitable candidates, assessing and selecting a company to acquire, making the deal and preparation of eventual combinations (Marks & Mirvis 2010, 53).

The acquisition motives are studied with the help of Trautwein's (1990) acquisition motive theories and more closely with the help of the efficiency theory, the valuation theory and the monopoly theory. In to the efficiency theory, acquisitions aim to achieve synergies by planning and executing acquisitions. Synergies can be categorized in financial synergies, operational synergies and managerial synergies. In the monopoly theory acquisitions are planned and executed to get market power and the valuation theory argues that managers have better information about the target's value in an acquisition than the stock market.

The acquisition strategy is compared against Porter's (1985) competitive strategy and corporate strategy. The acquisition strategy can be divided according to the characteristic of the companies that are acquired. Strategies can involve acquiring related or unrelated companies. (Harrison, O'Neill & Hoskisson 2000, 167).

3 RESEARCH DESIGN

This chapter presents the validity, reliability and trustworthiness of this study. It also describes the reasons behind the selection of the case company and how the data gathered for this study is analyzed. Also the framework is represented.

3.1 Research Approach

This study is executed by using a qualitative research approach. The research objective determines the research method. (Kvale 1996, 68; Ghauri, Gronhaug & Kristianslund 1995, 83.) The main reason for choosing a qualitative research approach for this study is the objective of the research. Hence the research problem is best solved through qualitative research methods. Because the objective of the study is to find out how serial acquirers select the companies they aim to buy and when the aim is to uncover and understand a phenomenon about which little is known qualitative research methods give sufficient answers (Ghauri et al. 2005, 110-111).

A case study is suitable, when studying issues in a single organization or smaller units within an organization. In a comparative case study the same issues can be studied in several organizations and then the findings may be compared with one another. This study focuses on an in depth study of one organization rather than on an comparative case study. (Jankowicz 1995, 179.) The time limited for this study was also a constraint towards choosing a comparative case study. Because this study is a single case study, its purpose is not to be representative of other cases. The first obligation of a single case study is to understand the study at hand (Stake 1995, 4). A case study method is used in a research, when studying a single organization and the aim is to identify, in a thorough way, factors inside the organization (Jancowicz 1995, 179). A case study approach is the best suitable method for the thesis, if the form of the research question is how and why, if the thesis does not require control of behavioral events and the thesis focuses on contemporary events (Yin 2009, 7). In this study a single case design is selected. There are five criteria for choosing a single case approach instead of a multiple- case design. Firstly, a single case approach is justified if one selected case meets all of the conditions for testing the theory. Secondly, one case is sufficient for a study, if it represents an extreme case or a unique case. Thirdly, one case can also be a typical case and therefore representative enough. Fourthly, there can also be a situation where the phenomenon has not been studied before and therefore one case is a revelatory case. Finally, a single case study is justified, if it is a longitudinal case study. In a longitudinal study the same case is studied at two or more different points in time. (Yin 2009, 39- 42.) This study is

made using just one case and it is justified, because it is a unique case and therefore sufficient enough.

A researcher that makes a case study needs clear research questions, a thorough understanding of the existing literature, a well- formulated research design and excellent language skills. Making a case study requires abilities to synthesize large amounts of diverse data and ability to communicate with both the subjects of the research and the readers that will eventually read the study. (Scapens 2004, 107.)

A case study is not a methodological choice, but the object to be studied is the factor that determines if case study is the right way to go. A case study is useful when the area of research is not well known. (Ghauri 2004, 109) When choosing a case or an object for a case study, the criterion is that the choices are consistent with the research problem. The case should also correspond to the theoretical framework that is being used. Other important issues are time available, financial resources and personal contacts. (Ghauri 2004, 112-113)

3.2 Case Selection

The primary objective of case study is not to understand other cases. The aim is to understand the case that is being studied. Selected cases can be typical cases or unusual cases. A typical case is usually representative, but unusual cases may illustrate matters that may not be noticed in typical cases. (Stake 1995, 4.) This case is a unique case.

The selection of the case company was relatively easy, because of the nature of the study. In Finland there are just a few companies that can be categorized as serial acquirers. The reasons for selecting KONE, was firstly the lack of other similar companies, but also because KONE has a history of making several acquisitions each year (Talouselama.fi/yrityskaupat).

Another selection criterion was the access to the company. The willingness of companies to sacrifice time and give information to a study should not be taken for granted. More frequently the execution of a thesis has not been possible because of the unwillingness of companies to co-operate. The accessibility to the case company is vital and the time and access for fieldwork is also almost always limited. An important criterion in the case selection is to maximize what one can learn from the case selected. (Stake 1995, 4.) Lack of data access can often cause problems and in worse cases delay the research or totally enable the execution of the research. (Jankowicz 1995, 32-33). When a company is willing to participate in a research, it gives up expensive management time and therefore access may not be granted lightly (Macdonald & Hellgren 2004, 267). Already having access to the case company, because of the previous cooperation between the university and the case company, was one of the criterions why this com-

pany was selected. The execution of the study was more certain when the access was already ensured (Fletcher & Plakoyiannaki 2011, 184-187).

3.3 Data Collection

The data for this study was collected from previous literature, company documents and an interview made with the vice president of KONE, Pekka Wikström. When using more than one method or technique in the same study, the approach is known as triangulation (Collis & Hussey 2003, 78; Jancowicz 1995, 175). There are four ways of using triangulation in a study: theoretical triangulation, data triangulation, investigator triangulation and methodological triangulation (Easterby-Smith, Thorpe & Lowe 1991, 133-134). In this study triangulation occurs by using data triangulation, which refers to data that is collected over different time frames or from different sources (Easterby-Smith, Thorpe & Lowe 1991, 134). In this case data is collected from different sources.

Interviews as a base for a study is well suited for three reasons: Firstly if the study is exploratory and theory building. In these cases the researcher may find new relationships or situations which may lead to new theories. Secondly if there is a small population of possible respondents and thirdly if the researcher wants to develop a deeper rapport with informants. This is not possible through written questionnaires. (Daniels & Cannice 2004, 186-187.)

In a case study, the most important source of information is an interview. The other sources are documentation, archival records, direct observations, participant observation and physical artifacts. (Yin 2009, 106.) Information gathered in an interview or other information gathered in the field should be guided by the research questions (Stake 1995, 50). The interview should be by all means well planned in advance (Stake 1995, 64). The interview made for this study is structured according to the research questions. The questions are divided using the sub questions as criterion.

The interview with Pekka Wikström, Vice president of KONE was made in Helsinki, at the KONE headquarters. At the interview were present the interviewer and the interviewee Pekka Wikström. The interview was made 25.11.2011. The location was a conference room without any disturbance. The interviewee was very relaxed and was willing to answer all the questions asked. The advantage of a face-to-face interview is that the interviewer is present and can amplify the meaning of the questions and the intentions behind the questions (Jancowicz 1995, 249).

When choosing the interviewee for a study, first the company has to be decided then the right person within the company has to be chosen (Daniels & Cannice 2004, 193). The interviewee was selected because of his knowledge and experience of the subject, so the selection of the interviewee was a deliberate and discretionary sampling (Puusa

2011, 76). A good interviewee is someone who is trustful, consistent, gives concise and precise answers provides coherent accounts, does not continually contradict themselves and holds themselves to the interview topic (Kvale 1996, 146). The interviewee in this study fulfills all the qualities and therefore is a trustworthy source of information.

Choosing the interviewee on the basis of the information given above is also called a key informant interview. This form of interview differs from other form of interviews, because the respondent is chosen on the basis of their specialized knowledge instead of being randomly chosen. The criterion for a key informant are their role, job title, position in the organization, their knowledge of the issue, their willingness to help and their perspective on the issue. (Jancowicz 1995, 212.)

The interview itself was a semi structured interview with structured questions, but the possibility for altering the order of questions and additional questions was left. This interview started with the interviewee freely describing the company and its operations. This gave some answers to the interview questions and also gave more data than only the interview questions would have given. A semi-structured interview differs from a structured and an unstructured interview in the sense that the topics and the people who are going to be interviewed are determined beforehand. A semi structured interview also minimizes bias in the results because of the way it is formed. The difference between a structured and a semi-structured interview is that in a semi structured interview the interviewed may answer with his/her own words. The selection of the form of interview should be based on the research problem. (Eskola & Suoranta 1998, 87-89.) A semi structured interview requires more skills from the interviewer than a fully structured interview, because it demands more flexibility and adaptability because the interview situation is not structured in advance (Jankowicz 1995, 201-203). A semi structured interview is effective when asking about feelings and attitudes, but especially when the range of possible answers is uncertain (Jankowicz 1995, 205).

The interview for this study was recorded with a tape recorder. Recording the interview helps the interviewer to concentrate on the topic and the dynamics of the interview. Other methods of recording an interview are videotape recording, note taking and remembering. (Kvale 1996, 160.) In the interview for this study options of methods were note taking or tape recording. The advantage of note taking during the interview would have been the immediate screening and summarizing of the information, which means that the analyzing of the data would have been immediate. The negative aspect of this would have been that the information could have been distorted and bias and errors could have occurred. (Collis & Hussey 2003, 193.) Therefore tape recording the interview was a more solid option.

A short interview, meaning an interview that lasts under 20 minutes, can be adequately covered by writing notes during the interview. Any interview that is longer than half an hour should be recorded. Because the interview with Pekka Wikström took ap-

proximately one hour and entailed a lot of information, it was justified to record the interview in its whole. Another issue that justified the use of a tape recorder was the interest of using word-for-word quotations that suited well for this study. This would have been impossible without a precise recording of the interview. (Jankowicz 1995, 206.)

The figure below clarifies the research problems for this study. The approach begins with the main research question “*What issues impact the selection of acquired companies from the point of view of a serial acquirer?*” and this main research question is answered by the help of three sub questions: “*What is a buying process for a serial acquirer like?*”, “*What are the motives for a serial acquirer to buy companies?*” and “*What is the connection between company strategy and serial acquisitions?*”.

Table 3 Operationalization of the research

Research question	Subquestions	Interview questions
What issues impact the selection of acquired companies from the point of view of a serial acquirer?	What is a buying process for a serial acquirer like?	Questions 1-9
	What are the motives for a serial acquirer to buy companies?	Questions 10-15
	What is the connection between company strategy and serial acquisitions?	Questions 16-24

The questions on the right hand side in the figure above are shown in the appendix 1. The questions are divided according to the sub questions. To further open the framework of this study, the sub questions can also be presented in another way. The table below shows the way these sub questions are approached and studied in this thesis. The sub questions are on the left hand side and on the right hand side the sources of information used to answer these questions. The acquisition process is describes by the help of literature, the RAID principles and the key person interview. The acquisition motives are distinguished through literature, Trautwein’s acquisition motives theories and the key person interview and the acquisition strategy is studied through literature and the key person interview

Table 4 Sub questions

Acquisition process (sub question 1)	Literature, RAID and interview
Acquisition motives (sub question 2)	Literature, Trautwein's acquisition motives theories and interview
Acquisition strategy (sub question 3)	Literature, interview

The acquisition process is studied with the help of previous literature, the RAID model that is presented by Cullinan, Rovit & Tymms 2003 and the interview made with Pekka Wikström, Vice President and Head of Acquisitions and Alliance at KONE. The acquisition process of KONE is then compared with the acquisition process of a successful acquirer or RAID. This way it can be recognized whether the acquisition process of KONE is compatible with an acquisition process of a successful acquirer. The acquisition motives are compared with three of the acquisition motive theories by Trautwein and the connection between the serial acquisition strategy and other company strategies is studied through existing literature and the interview with Pekka Wikström.

3.4 Data Analysis

When analyzing a qualitative data, the purpose is to clarify the collected data and through this produce new information. The aim is to compress the data to something clear and meaningful to enhance the information value of it without losing the information it contains. (Eskola & Suoranta 1998, 138.) In qualitative research the data is collected discretionarily and this is a characteristic that describes qualitative research. Because of this, a qualitative research is usually based on a relatively small amount of cases. In general in qualitative research the size of the data does not affect the success of a study. (Eskola & Suoranta 1998, 61-62.)

Field notes, such as direct tape recordings, must be first converted into write-ups that are intelligible products that may be understood also by someone else than just the researcher (Miles & Huberman 1994, 50-51). In this study the tape recording is transcribed into text, but any pauses or facial impressions are not written up, because they are not seen as an important source of additional information for this study.

The interview was made in Finnish, but key words that were used in the interview were translated into English, because of this there were no misunderstandings or use of wrong words when translating the interview into English.

The interview questions were divided according to themes. They were divided into questions about the acquisition process, the acquisition motives and the acquisition strategy.

3.5 Trustworthiness of the study

A study has a good reliability, if the same study can be done over again and in the later study the same results would occur. Good documentation of the study also strengthens the reliability of a study. (Yin 2009, 45; Collis & Hussey 2003, 58.) In this study reliability is high, because if the same questions were asked from the interviewee, most likely the same answers would occur. The questions cannot be interpreted in a different way by another interviewer. The only difference would arise, if the same questions about the future of the company would be asked in a later study. But hence this study aims to describe the current situation of the company and its acquisition motives; this does not affect the reliability of the study.

In an interview, validity is an important issue, when deciding if the interview is suitable for the study or not. A valid argument is sound, well grounded, justifiable, strong and convincing. Validity can also be measured by asking a question: “Are you measuring what you think you are measuring?” (Kvale 1996, 236-238). Validity can be undermined because of research errors; faulty research procedures, poor samples and inaccurate or misleading measurement (Collis & Hussey 2003, 59). The interview made in this study can be considered valid, because of the background of the interviewee and because of the way questions are based on the theory used as a basis for this study.

Trustworthiness of a study can also be measured by the objectivity of a study. In this study objectivity should be viewed in the case of objectivity of the interview made in this study. Objectivity has three concepts: freedom from bias, intersubjective knowledge and being adequate to the object. The first refers to reliable knowledge that is undistorted by personal bias. The second is about scientific data being intersubjectively testable and reproducible. The last concept is about letting the object speak. (Kvale 1996, 64-65). The interview made in this study fulfills all three concepts: there was no personal bias by the interviewer in the interview, because the interviewer has no personal interest to the outcome of the study or no previous connections to the case company. Secondly the interview can be reproduced by interviewing the subject again and asking the same questions. The answers given in the interview were not connected to the time the inter-

view was made. In the interview the interviewee could also speak freely without interruption or by leading the interview.

The trustworthiness of the interview can be studied from different perspectives. Firstly an interview is always interactive and the parties participating in the interview always affect each other, therefore because the interview is started by the interviewer, he or she leads the conversation to some extent. This affects the trustworthiness of an interview. Secondly an interview is always a subject's interpretation about issues, events and phenomenon. These issues affect the trustworthiness of an interview, because this makes a study a social construction. (Puusa 2011, 73.)

Leading questions may also affect the trustworthiness of a study. This is a widely recognized problem. (Kvale 1996, 157.) In this study the wording of the questions used in the interview is neutral and no leading questions were asked.

Recording an interview can sometimes affect the trustworthiness of a study. The recorder can affect the interviewee and provoke anxiety and nervousness. The problem does though not occur when dealing with top executives, because they are used to speaking publicly. (Hart 1991, 196.) Because in this study the interview was made with a top executive, any nervousness or anxiety could not be detected. Therefore the trustworthiness of this interview, in regard of the recording device, cannot be questioned.

This study is mainly based on one interview. The reason for selecting only one interview is focusing more on quality than quantity. This is also in line with the present approach that emphasizes the quality rather than the quantity of the interviews (Kvale 1996, 103). The interview is made with an expert of the subject. To determine if the data size is adequate it can be tested by seeing if the data is saturated. The data is saturated if new cases or interviews do not produce any more information that would be relevant for the research question (Eskola & Suoranta 1998, 62). In this case there would not have been any other persons in the company that could have been interviewed and that would have had more information about the subject than the expert interviewed for this study. Considering this, the data is saturated with one extensive interview with a key person.

The main limitation of this thesis is the use a single case approach and therefore the narrow ability to widely generalize the study to apply to other similar cases. Because the study is a one case study, it is also bound to the industry the case company operates in. The industry restrains the generalization of the results to other industries. Even if the study has its limitations, the aim is however not to generalize the findings. These limitations may though further more comprehensive studies about the subject.

The use of only three of seven of the acquisition motives gathered by Trautwein may also be seen as a limitation. For a more comprehensive study all of the theories could be studied in one case company or in multiple companies. In this way a wider perspective of the theories could be produced. The problem with some of the theories left outside

this thesis is that they are very difficult to study. This is the reason why these theories were left outside this thesis.

4 ACQUISITION TARGET SELECTION BY KONE

The case company is studied from three points of views: its buying process, its motives to acquire companies and the connection between acquisition strategy and other strategies of the company. The case study is based on a key person interview.

4.1 Case company: KONE Oyj

KONE is a Finnish company that produces and maintains elevators and escalators. It is one of the global leaders in the industry. The company was founded in 1910. In 2011 the company had on average 35 000 employees. The company has 1000 offices around the world, eight global production units located in their main markets, seven global research and development centers and authorized distributors in over 60 countries. (Kone.fi: KONE in brief.) Because the company's businesses affect the whole world, it can be categorized as a global company (Oxford dictionary 2005, 659).

KONE's turnover in 2011 was 5 225.2 million euro and in the time period January-June 2012 it was 2 785 million euro. The turnover of KONE consists of maintenance, modernization and manufacturing of elevators. (KONE interim report³ 2012.) Other businesses KONE is involved in are escalators, auto walks, automatic doors, and monitoring and access control systems. (Kone.fi: KONE in brief)

In 2011 capital expenditure in acquisitions was 185.3 million euro (KONE interim report 2012.). Acquisition of Canadian CNIM Canada Inc. and the increase of shareholding in GiantKONE increased the presence of KONE in both Canada and China. (Kone.fi, KONE in Brief).

KONE is a serial acquirer and the company has made a vast amount of acquisitions since it was founded. After 1968 and the acquisition of Asea-Graham elevators the internationalization process of KONE started. First the leadership in Scandinavian markets was reached and after this in 1975, through the acquisition of Westinghaus, the volume of business doubled and the expansion continued to Europe. International market leadership in escalators was reached in 1996 through the acquisition of the rest of the shares in O & K Rolltreppen. Global elevator and escalator business alliance was established with Toshiba. (Kone.fi, Internationalization.)

KONE makes 20-30 acquisitions a year and publishes all acquisitions, that are valued over five million euro. The amount that exceeds the five million euro limit is usually

³ Financial statements issued for a period less than a financial year. (A Dictionary of Finance and Banking, Oxford)

about 6-8 acquisitions a year. The average acquisition is valued between 3-5 million euro and the turnover of the traditional acquisitions made in one year is about 100 million euro. These figures are average figures and may vary depending on the year. The company makes mainly small acquisitions and only a few larger a year. Because of these characteristics KONE can be categorized as a serial acquirer.

For this research one key person, Pekka Wikström, Vice President of KONE, was interviewed. He is positioned at KONE headquarters in Helsinki, Finland and is head of Alliances and Acquisitions. He has been working for KONE since 2006; first as Assistant Vice President and since 2009 as Vice President. After graduating from Helsinki School of Economics, he has worked as a consultant at McKinsey & Company Inc. and in the banking industry.

The information presented in this chapter is based on the interview made with Pekka Wikström 25.11.2011.

4.2 The buying process of KONE

The buying process of KONE, which is a serial acquirer with several acquisitions a year, is described below. Firstly the sources of finding suitable companies to be acquired are described. Secondly the duration of a buying process and thirdly the decision making process that involves the decisions from the selection of suitable companies to the decisions that are required for making the deal.

The figure below shows how the acquisition process of KONE goes in a cycle. This can be assumed because of the amount of acquisitions made. Because of this the routines are strong and the learning is an ongoing process. In practice KONE may have overlapping acquisitions and so the processes are also overlapping.



Figure 6 Acquisition process of KONE

The decision process starts with the narrowing of possible candidates for acquisitions, usually through a market research, to a list of suitable targets. After this the selection of the target is made. If the acquisition is made in another country, both the headquarters and the offices in the country where the acquisition is made have to agree on the acquisition. Commitment to the acquisition of the offices in the target country is crucial for the success of the acquisition. When the target company is selected, KONE uses standardized tools to measure and analyze the profitability and possible synergy advantages of the acquisition. If the acquisition still appears lucrative and sensible the decision is made to proceed with the acquisition. The decision making process is divided according to the size of the acquisition. The larger the size of the acquisition, the higher the decision making level. After the approval of the acquisition, the acquisition is made. The duration of the acquisition may vary and the definition of the acquisition, where it begins and ends, is also debatable. The pre acquisition phase may take many years, but the process is not necessarily active through the entire period. The importance of acquisition follow up is recognized at KONE. After every acquisition data is collected and analyzed, to some extent, and this information may be used to improve the efficiency of future acquisitions.

4.2.1 *Finding the companies*

In most cases KONE is the initiative party in an acquisition, meaning that KONE is the one that approaches the company it wants to acquire. Usually the process starts from

selecting suitable candidates for an acquisition from a list of 30- 40 companies. The first contact can be made in various ways: sending a letter from KONE, making a call, inviting the other party for lunch and discussing the proposal or using a third party, for example requesting a law firm to send a letter in the name of an undisclosed principal⁴. All of these ways produce the first contact. There is a cultural difference in the way the first contact is achieved. For example in the United States it is not unusual for the target company to use an advisor and then contact the local representative of KONE. There the seller is more the initiative party.

Maybe five cases (in Finland) have been such, where the sellers (target company) have taken themselves advisors and then called us (Wikström, interview 25.11.2011).

After the first contact the majority of companies accept the proposal for further negotiations. After this it is crucial to be in a face-to-face contact with the target company.

--sending emails is not a possibility. Then later on we can exchange information via email, but the negotiations have to be done always face-to-face. (Wikström, interview 25.11.2011.)

Sometimes the companies that are contacted are not willing to sell. After the first contact the relationship to the target company is still being sustained.

We are trying to sustain the relationship in some way. For example we contact them again after a year, go for lunch and ask them again if they are willing to sell. If they still are unwilling to sell, we meet them again after a year and ask them the same question. Roughly speaking. (Wikström, interview 25.11.2011.)

Very often the situation where a company is acquired is an irregularity in the business of the acquired company. Irregularities can be situations where the owner wants to retire and his or her children are not willing to continue the family business, the company is in an economic crisis, the company has grown too much and the owners are overwhelmed or the company has invested too much and is unable to finance the new investments.

⁴ A person who buys or sells through an agent or broker and remains anonymous. (A Dictionary of Finance and Banking, Oxford)

Or, sometimes the sellers just want money (Wikström, interview 25.11.2011).

Sometimes reasons behind selling a company can be as simple as the owner wanting to leave the stress of being an entrepreneur.

Being an entrepreneur has its own risks and troubles. They want to sell their company and instead just work for KONE. They get money for selling their company, but they can still continue being in the business without worrying about it and having the risk of being an entrepreneur. (Wikström, interview 25.11.2011.)

Usually at the time, when companies suited for acquisition are selected, KONE and all of its rivals have the same information about the companies. In some rare cases KONE may have more information about the company it is considering acquiring. This may happen for example in a situation where a former employee of the acquired company has come to work for KONE and has some inside information about the company. Usually KONE does not have more information about the acquired companies than any of its rivals have.

Before the first date we have the same amount of information about the target company as our rivals. But at some point of the process substantially more than the market. (Wikström, interview 25.11.2011.)

It is understandable that the acquirer has more information about the acquired company at some point of the acquisition process, because they obviously need to have access to the information about the acquired company to be able to decide whether to acquire or not.

4.2.2 Duration of an acquisition

There are two factors that affect the duration of the buying process of KONE. Firstly the process is much faster, if the acquired company has sold something before and is familiar with the acquisition process. Usually companies that sell for the first time do not know how to find the data needed and do not use advisors. Secondly KONE makes simultaneously many acquisitions and because of the overlap resources are limited. A buying process for a serial acquirer takes on average 5-6 months. The acquisition pro-

cess may also take only 2-3 months, but this is unusual. In situations where the acquisition process is this short, the owners of the acquired company are private equity owners and have been preparing the company for an acquisition. They have done their due diligence, are in a hurry to sell and often have an advisor.

For an acquirer this is an easy acquisition (Wikström, interview 25.11.2010).

Sometimes acquisitions can take much longer. One of the longest acquisitions has taken three years. But the interpretation about the duration of an acquisition process may vary, because sometimes the process may start with a discussion about the acquisition, but the actual acquisition may take place ten years later. So the process is not active all the time. Sometimes there may be a brake for months before the next contact.

It's not like we call each other every day (Wikström, interview 25.11.2010).

The typical target for an acquisition is a company that is involved in the core business of the buying company. In the case of KONE this is elevator maintenance. Core businesses for a company are those which are in a lucrative industry, can achieve potential competitive advantages, are importantly connected with other business units and provide skills or activities that can be diversified (Porter 1987, 58). Due to the core business and continuous buying processes the acquisitions rarely fail and are relatively fast. For KONE the main reason for the company's high success rate is that they make, in their opinion, easy acquisitions. KONE describes an easy acquisition to be an acquisition, where a company buys another company that is involved in their core business and is much smaller than the buying company. The acquisition is hence very simple and can be managed as previous acquisitions made by the company. Here the routine of making serial acquisitions plays a significant role. The acquisition processes of KONE are tasks that are done with routines that have formed over time. These routines reduce the time needed for the acquisition process and raise the likelihood for acquisition success. This advantage is also recognized in literature by Laamanen and Keil (2008). They argue that routines and capabilities over time help a company to digest large numbers of acquisitions (Laamanen & Keil 2008, 665).

Overlapping acquisitions may delay the acquisition process of all the ongoing acquisitions. In a situation where there is a shortage of resources, KONE delays the other acquisition to avoid overlap.

The first 50- 100 days is the time when the acquisitions need most of our resources. – The process has its own challenges when there are overlapping acquisitions at this time. (Wikström, interview 25.11.2011.)

KONE has dedicated resources only in the United States, Spain and Italy that inclusively focus their operations in making acquisitions. Sometimes overlapping acquisitions in other countries are delayed because of lack of resources in the head office.

It's usually okay for the sellers. They neither are in a hurry. (Wikström, interview 25.11.2011.)

Acquisitions, where neither the acquirer or the acquired has a need to quickly make the acquisition, there is no pressure to speed the acquisition. In these cases it is more justified to complete the acquisitions that are urgent and proceed with the waiting acquisitions with more time.

4.2.3 Decision making process

The decision making process of acquisitions in KONE is structured and follows more or less the same steps in every acquisition. The company uses standardized tools to help the decision making. One is a financial model that locks all other cells, but the input cells that have to be filled with the information of every new acquisition. It is a standardized program, which has a standalone model that shows how the acquired company would develop, if it was not bought. This is a process that has to be done for every acquisition and it also shows the synergy advantages the company will gain with the acquisition. The other standardized tool the company uses is a standardized template, a word template, which contains all the quantitative information about the company. This mitigates the decision making process, because all parties involved in the process receive the information in the same format. If the company would not use a standardized template, every proposal would be different. The use of a standardized template is a matter that KONE sees as a field where they have succeeded well.

KONE has many offices located all around the world. In the case of an acquisition, the offices located in the target area have the responsibility of finding and approaching the target company and make the decisions in the early stages of the acquisition. The offices have the information needed about the acquired company, because usually the companies acquired are competitors of KONE in the area. Sometimes if the acquisition process has been challenging, KONE has ordered an independent company to do a market research to assist the decision making process. The research is made by an inde-

pendent consultancy company which identifies the targets in the area. After this the coordination of the acquisition is made in cooperation with KONE and its subsidiaries. The acquisition process continues when KONE produces a list of companies to acquire. After this the office in the target area prioritizes the companies and chooses the ones they start to approach. Once a year KONE gathers a target list from each subsidiary, where all the potential companies for acquisition are listed. Then KONE analyses the data and encourages the offices to choose the targets and to put them into the next year's budget.

The main reason for making these lists is to find the companies that are in the market area that is not dominated by any big players⁵ (Wikström, interview 25.11.2010).

When the acquisition reaches the point where decisions about the acquisition price, profitability etc. has to be made, the approval involves many parties. First of all, the Areal Director in the target country has to be in favor of the acquisition. Otherwise the acquisition will not be made. There has to be a commitment of the office to the acquisition. Otherwise there may appear uncertainty and blaming towards the headquarters in a case of acquisition failure. The next level of decision making is made by the Managing Director of the area where the acquisition is made. KONE has divided their global business in five areas. These areas are Africa, Americas, Asia/Oceania, Europe and the Middle East. Each area has a Managing Director. For an acquisition to be approved, both of these directors, the Areal Director and the Managing director, have to be in favor of the acquisition. Usually if the Areal Director approves the acquisition, the Managing Director is in agreement. In the figure below there is a chart of KONE's organization. The two uppermost, Service Business and New Equipment Business are the two business lines in the KONE organization. Below these are the five geographical areas that the organization is divided in.

⁵ Schindler, Otis, Thüssen

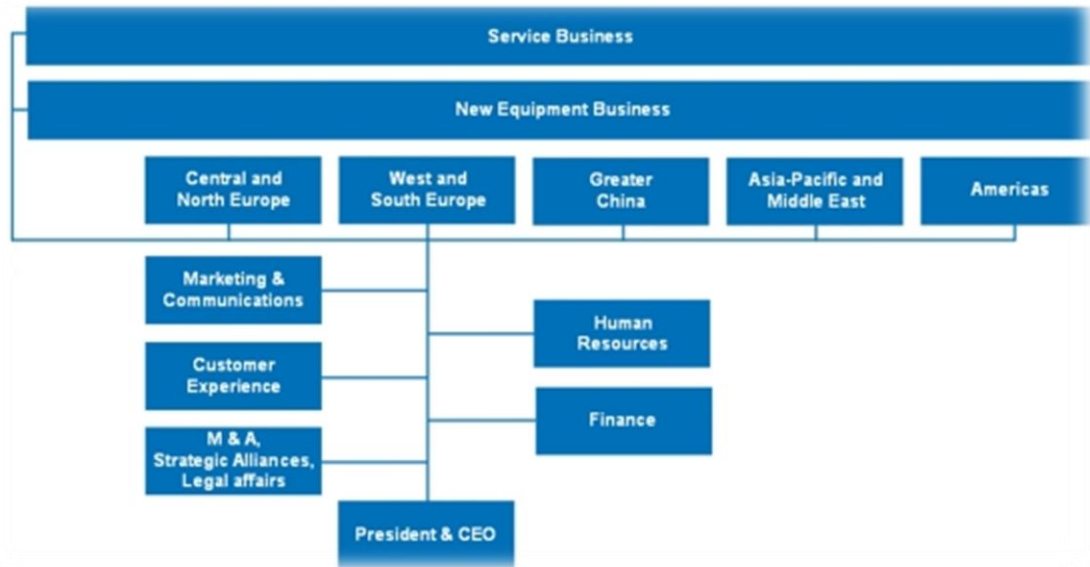


Figure 7 KONE's organization (Kone.fi; Organization)

Furthermore the organization is divided in Marketing and Communications, Human Resources, Customer Experience, Finance, Merger and Acquisitions, Strategic Alliances, Legal Affairs and at the bottom of the chart are the President and Chief Executive Officer. Mergers and Acquisitions, Strategic Alliances, Legal Affairs, Finance, the President and the CEO are involved at some point in the decision making process of an acquisition depending on its size and significance. The decision making process has size limits that decides the level of approval.

Table 5 Acquisition approval

Acquisition size (million)	Level of approval
< 5	Managing Director of the area
>5	Executive Board
>50-70	Board of Directors

If the acquisition value is less than five million euro, the Managing Director of the area, where the acquisition is made, approves the acquisition. When the acquisition value exceeds five million euro, the decision is made by the Executive Board. The third limit in the approval process is 50-70 million euro. When the acquisition value exceeds this limit, the decision has to be approved also by the Board of Directors.

All the proposals for acquisitions are checked by one person in the company, the Head of Acquisitions and Alliances, before they are further passed on to the department or person that makes the decision needed at different stages of the acquisition. Many times the Head of Acquisitions and Alliances is also involved in making the acquisitions, so the involvement is more long term.

4.3 KONE's motives to buy companies

A serial acquirer has three motives to make acquisitions: strengthen their core business, expand to new geographic areas and to buy out competition. In the case of KONE and the elevator business they are in, the competition has been bought out many years ago. There are four global players left in the industry: KONE, Schindler, Otis and Thyssen and therefore strengthening their core business and expanding to new geographic areas are seen as the main motives to make acquisitions. Hence the acquisitions made by KONE can be categorized in two different ways: KONE buys maintenance companies, which constitutes 95 percent of all acquisitions, and companies in the same business to expand to new geographical areas, which are more occasional. Below is a figure to clarify the motives KONE has at the moment to make acquisitions.

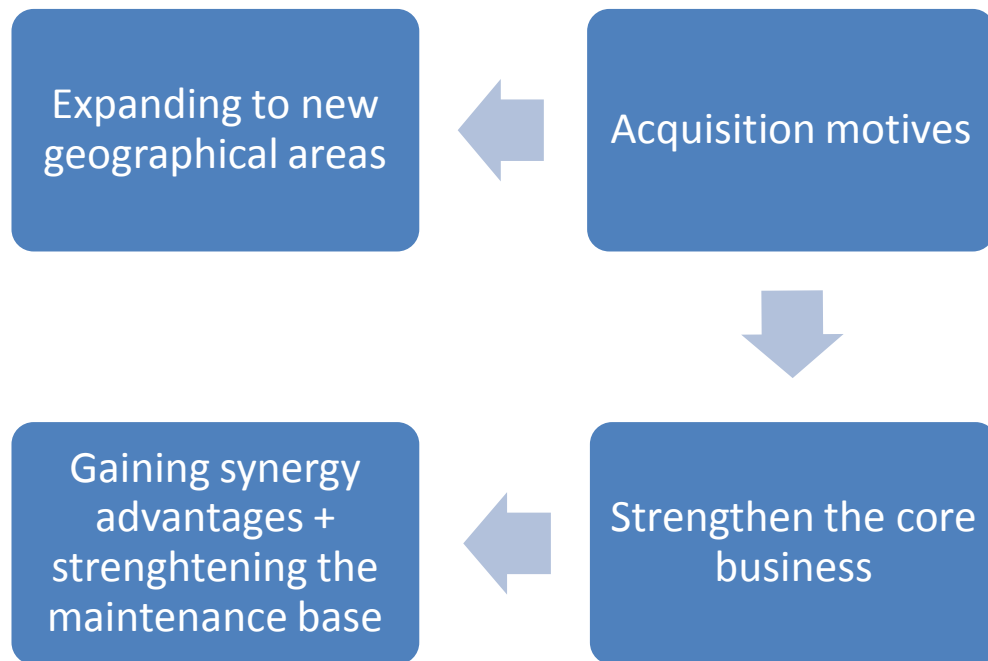


Figure 8 Acquisition motives of KONE

The advantages KONE achieves of strengthening their core business through acquisitions are synergy advantages and the ability to strengthen their maintenance base. Strengthening the maintenance base means that the base is more comprehensive after an acquisition, because of the acquired maintenance routes.

4.3.1 *Strengthening the maintenance base*

The motivation behind buying maintenance companies has two reasons. Firstly the company wants to expand its maintenance base by buying new companies. It does it by organizing and combining old and new maintenance routes. A company is often bought because of its maintenance, but the companies that are acquired usually have own business in elevator modernization and selling. KONE is mainly interested in the maintenance and modernization of the new company and sees the manufacturing part as a compulsory thing that has to be bought. Usually this part is calculated to be lost in the transaction. Secondly synergy advantages are substantial when buying new companies.

An acquisition can be very beneficial for the acquirer and one of these benefits are synergy advantages. When a company is acquired, it has its own administrative resources; offices, accounting systems and insurances, which are then joined with KONE's own pool. The majority of these acquired administrative resources are unnecessary and therefore the synergy advantages are sometimes substantial. Therefore the post-acquisition synergy advantages are bigger than the pre-acquisition synergy advantages a company has, before it is acquired. Other advantages are hard to measure,

because the acquired company does not exist after the acquisition and therefore there is no data that the advantages can be compared with.

After a successful acquisition the office in the area where the acquisition is made should be relatively more profitable and in the contrary when an acquisition is unsuccessful, the office should relatively perform less profitably. The problem in measuring the profitability of a single acquisition is problematic, because the size of KONE offices compared to the size of the acquired companies is substantially larger. The impact on profitability of a single acquisition made by one of KONE's offices is around 0.1- 0.2 percentage.

The acquisition sort of disappears in the numbers after the acquisition. We have thought about how we could follow up the profitability of a single acquisition, but it is quite impossible. To follow up the integration itself is something we have not seen to be very beneficial. (Wikström, interview 25.11.2011.)

There is a question about the benefits of following all the acquisitions and the costs of following them. KONE sees that the costs exceed the benefits and therefore closely following up all acquisitions is not considered beneficial.

4.3.2 Expanding to new geographical areas

KONE makes approximately one acquisition a year, where it expands to a new geographical area. The area can be a new country or an area inside a country, where KONE is not yet present. These areas can be found for example in the United States or in Spain and they are called white spots.

When KONE expands to a new geographical area, making a greenfield investment⁶, the logic is slightly different. In a new geographical area, the business of new elevators is in a bigger role. Also when acquiring in a new area, the acquisition entails the entire elevator maintenance portfolio of the acquired company. A Green Field investment is usually challenging, because the use of the maintenance base can sometimes be ineffective.

⁶ A project that starts from scratch, e.g. building a factory on a virgin site in the country. (A Dictionary of Finance and Banking, Oxford)

KONE is already so global, that expanding to new geographical areas is very insignificant. The only areas internationally, where KONE is not yet present is South America and in some African countries. Expanding to new geographical areas is much easier than expanding to new business areas. There is a different logic in them.

It usually goes wrong if a company expands all the time in all directions (Wikström, interview 25.11.2011).

When making acquisitions to expand to new business areas is very challenging and usually these acquisitions are very vulnerable for failure. Also making different kind of acquisitions, meaning both geographical and to new business areas is challenging and sensitive for failure.

4.4 Company strategy and serial acquisitions

The connection between company strategy and serial acquisitions is obvious. Making acquisitions for a serial acquirer is part of their company strategy and is a part of normal activities in the company. Making acquisitions is very structured and follows patterns that have developed over years. Acquisitions for KONE are part of their business, growth strategy and a way to develop their core business.

Our acquisitions are quite operative. It's not like in some companies where making acquisitions is exiting and special. For us it's part of our business. We make so many of them and it's a way to grow. (Wikström, interview 25.11.2010.)

The mindset of making acquisitions is different at KONE than it is in other Finnish companies. Making them is nothing out of the ordinary.

4.4.1 Acquisitions as a strategy

Acquisition strategy depends on the business area. Serial acquisitions cannot be made in the same scale in all business areas. Because of large scale maintenance business in KONE and the business area they are in, they are able to make so many acquisitions.

I have an acquaintance working in an accounting company. This company has bought many smaller accounting companies and it seems that they

have the same logic as we do: trying to get a better geographical cover for the business. (Wikström, interview 25.11.2011.)

There are not many other Finnish companies that can connect the same acquisition strategy to their business strategy as KONE can. Usually acquisitions made by other Finnish companies are investments for expanding their business and they are more occasional acquisitions instead of being part of their core business. Some Finnish companies usually make acquisitions in the early stages of their internationalization. The internationalization then occurs by expanding to new geographical areas through acquisitions.

In my opinion these are more challenging acquisitions. Both geographical acquisitions, as the expansion (through acquisitions) to another business area. (Wikström, interview 25.11.2011.)

Acquiring companies is part of KONE's business strategy. This is not an exception and can be recognized in other companies too. For example acquisitions are common in the banking industry and some banks acknowledge making acquisitions as a part of their business. (Streeter 2007, 38). For KONE making acquisitions is a normal activity. But it is not something they make just because they are used to making them. They also see that the prices they pay for acquisitions have potential to create more value.

I don't think we pay too much for the acquisitions and in my opinion we get the benefits of them that we intend to get. Making acquisitions is normal for us, but we don't do them just for the sense of making acquisitions. (Wikström, interview 25.11.2011.)

KONE makes several acquisitions at the same time. Overlapping acquisitions are not a challenge if the acquisitions occur in different countries, because the integration of the acquisitions is entirely at the responsibility of the offices in the target area.

We have given the offices tools, like a checklist, that they can use. Then we require an integration plan when the deal is approved. (Wikström, interview 25.11.2011.)

KONE head offices do not follow up the integration process of the acquisitions made by offices in other countries. They recognize that there might be some benefits of closely gathering and analyzing all the information about the integration processes in every

acquisition. They have thought knowingly left this monitoring at the responsibility of the offices in the country where the acquisition is made.

We do not follow up the integration processes (at the head office) of all the acquisitions, like some Finnish companies do that have someone at the head office monitoring the progress of all the integrations. This would again require its own resources. We do not see that the benefits of all this reporting would validate the effort. (Wikström, interview 25.11.2011.)

The integration process in acquisitions made by KONE is relatively simple because of the nature of most of their acquisitions. KONE acquires mainly maintenance companies and therefore the integration process consists more of administrative operations. The process of integrating smaller acquisitions, which usually are maintenance companies, is substantially easier than the integration process of a large acquisition.

The nature of acquisitions made by KONE also affects the success rate of their acquisitions. Because KONE makes so many easy acquisitions, their success rate is also very high. About 90 percent of their acquisitions are successful. In comparison to some research (e.g. Marks & Mirvis 2001, 80) on average over 75 percent of all acquisitions fail. This depends though on the way success and failure is measured in an acquisition. The main reasons for the high success rate of KONE acquisitions are that companies acquired are in the same business, they are substantially smaller companies and the process of making acquisitions is already very established. In this process includes for example the acquiring itself and the defining of the value of an acquisition.

We are actually quite careful with our acquisitions. We rather walk away than pay too much for an acquisition. If we expand to a new geographical area we pay extra attention to the acquisition. (Wikström, interview 25.11.2011.)

For KONE an unsuccessful acquisition is for example an acquisition that is made to expand to a new geographical area and then some of the new market area has been lost or the expansion in the new market area has not been as successful as planned. An acquisition can also fail if there has been some information that has not been discovered during the due diligence or negotiations and that has had an impact financially.

If you never make unsuccessful acquisitions, you probably make too few of them (Wikström, interview, 25.11.2011).

In a sense it can be interpreted that some acquisitions fail regardless. There is also an atmosphere that it is allowed to fail in some acquisitions, because the average success rate of acquisitions is very low.

4.4.2 *Changes in acquisition strategy*

In the beginning of KONE history, the strategic meaning of making acquisitions was very different from what it is today. But acquisitions have always been a part of KONE's strategy and a way to expand. In the beginning of KONE's history the situation in the industry was, that you had to acquire others or you were acquired yourself.

In the past, when KONE was expanding, the idea was that you had to eat or be eaten. (Wikström, interview 25.11.2011)

First KONE expanded in Scandinavia by acquiring Asea-Graham elevators and after this the expansion to Europe started with the acquisition of Westinghaus. Then the expansion continued globally. KONE expanded mainly through acquisitions. Some green field investments were made.

The logic (of acquisitions) was totally different in those days. They just wanted to go out to the world. Now the logic is more in growing the density of the maintenance base and through this gain operative advantage. (Wikström, interview 25.11.2011.)

Today the industry does not change as drastically, because all the remaining global competitors (Schindler, Otis, Thüssen) in the industry are too large to be acquired. The only way the industry would change, if two of the global competitors would merge.

The acquisition strategy is not likely to change in the following five years, unless KONE would decide to expand outside the industry. If KONE would for example invest more in its small door business in addition to its elevator, escalator and auto walk business, the logic would change. There has been some discussion about the direction where KONE should go, if they should start to do something else, but at the moment the acquisition strategy is not likely to change because of the nature of the industry.

Acquisition strategy can also involve enhancing the image of a company by buying companies that improve the company image. Globally acquisitions made by KONE do not affect the company image, because of the size of the acquisitions. Even larger acquisitions have mainly a local impact on the company image. After an acquisition KONE

keeps some of the acquired companies separate or in some cases keeps the brand of the acquired company alive. The main benefit, image ways, when acquiring a company may be that the company has good customer relations. This benefit may be gained through an acquisition. To acquire a company mainly because of enhancing KONE image is not needed.

KONE is a good brand. It is known everywhere. (Wikström, interview 25.11.2011.)

The benefits of keeping the brand of an acquired company alive after the acquisition is not seen as an important issue, mainly because of KONE's own brand. The brand of KONE is strong and known globally.

5 DISCUSSION AND CONCLUSIONS

The aim of this study was to study the issues that impact the selection of acquired companies of the point of view of a serial acquirer. The main research question was further studied through sub questions about the acquisition process, acquisition motives and the linkages between acquisition strategy and other company strategies. This study concentrated on one case company KONE. The motives of making acquisitions were further reflected through the acquisition motive theories by Trautwein 1990. In this chapter the results and the theory are brought together and discussed.

The buying process of KONE is in this thesis studied from three perspectives: the finding of the target companies, the duration of the acquisition and the decision making process. *Serial acquirers like KONE make relatively easy acquisitions and this part affects the acquisition outcome.* This is one of the most important factors behind the success factor in acquisitions of a serial acquirer. A buying process for a serial acquirer is very standardized and follows mainly the same patterns as the previous acquisitions made by the company. These routines reduce time and raise the likelihood for acquisition success (Laamanen & Keil 2008). There is also a high degree of learning from previous acquisitions, mainly because of the reporting of the acquisition process. The reporting is though limited in the way that costs of reporting do not exceed the benefits (Wikström, interview 25.11.2011).

There can be recognized similarities in the acquisition process of KONE and the RAID principles (Cullinan, Rovit & Tymms 2003) of a successful serial acquirer. These two figures may in fact be combined, which on its behalf implies that the acquisition process of KONE is successful.

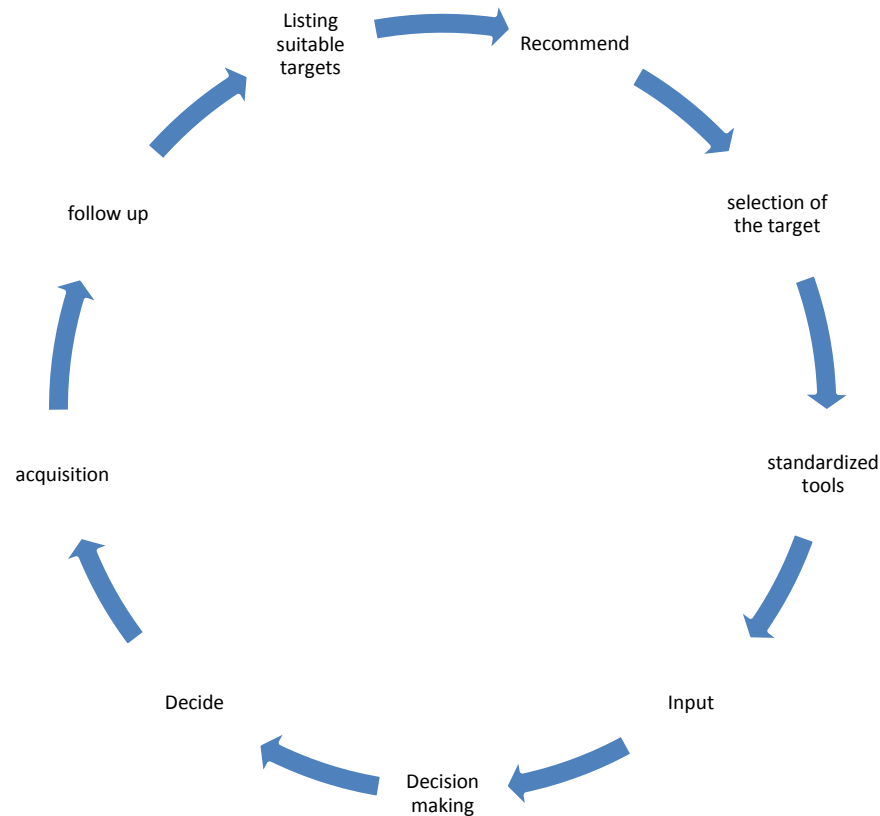


Figure 9 A successful acquisition process

The way the acquisition process is managed is also in some parts similar in RAID and at KONE. In both cases there is one person, or a team, that is involved in the entire acquisition process of all the acquisitions. At KONE this person is the Head of Acquisitions and Alliances.

There is a wide range of acquisition motives that vary from desire to increase market power to diversifying the company (e.g. Lees 2003,3-4-; Anderson et al. 2001, 575). *The main motive for KONE to make acquisitions is to strengthen their core business instead of growing their business. 95 percent of their acquisitions constitute of these acquisitions. The other motive at the moment is to expand to new geographical areas.* The motives behind the majority of acquisitions, which are buying maintenance companies, are the strengthening of their core business, which is maintenance of elevators, and to gain synergy advantages when integrating the acquired companies to KONE. The acquisition motive of a serial acquirer differs over time, but in the case of KONE the motives to make acquisitions is unlikely to change in the next five years.

It seems that in the case of a serial acquirer that has made several acquisitions during a long period of time the acquisition motives have been narrowed down and settled in a segment of company operations where it is most productive. In the case of KONE the most efficient way to utilize acquisitions is to grow the maintenance base through them.

The alternative way for growing the maintenance base would be to establish own maintenance routes and having to compete with other companies that are in the business of elevator maintenance in the same area. This would be a more costly alternative. Even though the majority of acquisitions made by KONE are small acquisitions, there are continuously acquisitions that are substantial and for their part still grow and establish the presence of KONE in the global markets (Kone.fi, Internationalization).

Trautwein's efficiency theory states that acquisitions are made because of synergy advantages. These synergy advantages can be divided to financial synergies, operational synergies and managerial synergies. (Trautwein 1990, 284.) Efficiency is also seen as an important driving force behind acquisitions (Lees 2003, 33). *In the case of KONE operational synergy advantages are at the core of their motives behind acquisitions.* The synergy advantages KONE gains through acquisitions of maintenance companies are substantial. The synergies are gained through the organization of new maintenance routes and the limitation of overlapping processes. For example the administrative resources of an acquired company are not necessarily needed after the acquisition, because KONE may use its own existing resources. Operational synergies are achieved by combining operations or units that have previously been separate (Trautwein 1990, 284). By comparing the results of the case study of KONE and the efficiency theory, it can be concluded that in this case acquisitions can be motivated by operational synergy advantages.

According to the monopoly theory (Trautwein 1990, 285-286), building monopoly power in the market is the driving motive for acquisitions. This can to some extent be supported in this study, but also some results are controversial to the theory. *The main concern when comparing the statements of the theory and the findings of the case study is that in this particular industry acquiring market monopoly is not possible any more* (Wikström, interview 25.11.2011). Findings that would promote the theory would be that the case company would possibly acquire other companies in the industry to reach a monopoly position, if it was possible. But the size of other companies having a substantial foothold in the market is too substantial for an acquisition. On the other hand, the theory also implies that acquisitions are made to get market power, even if it would not lead to a position of monopoly in the industry. This can be achieved for example through collusions with competitors. This is something KONE has done and for this part the monopoly theory has its grounds.

The main observation that can be made concerning the monopoly theory is that it is unlikely that acquisitions are made purely because of desire to achieve a monopoly position in the market or even because of a single desire to achieve market power. There are most likely also other motivators behind acquisitions and building monopoly power as a single motive is too weak to make acquisitions.

Valuation theory argues that managers of the acquiring company have unique information about the value of the benefits an acquisition would produce or they have discovered an undervalued company (Trautwein 1990, 286-287). *In the case of KONE it is very unlikely that there has been any hidden information they have possessed in an acquisition.* Usually acquisitions are made with the same information the market has. Yet there have been some rare cases where private or better information about a company that is considered for acquisition has been possessed by KONE. This is a very vague argument for the valuation theory because in these rare cases the value of the hidden information has not been that high. A typical case has been a situation where an employee of KONE has previously worked at a company that is being acquired and therefore may have some information about the target company that the market does not have. Because of this, the valuation theory does not get sufficient support from this study.

In other studies (e.g. Wensley 1982) private information is also recognized to be ambiguous. This brings out an aspect that even if a company would possess private information or better information about a target company, the use of the information can vary. Sometimes the information may be useless for the company that possesses it, but have high value to another company. Private information was not regarded as a highly important issue in the case company KONE. Therefore in this case the presence of private information would not likely be a motive behind acquisitions.

The acquisitions made by a serial acquirer are usually linked to other strategies of the company and are part of normal activities. Acquisitions for a serial acquirer are equally important strategic issues as any other issues in the company. *In the case of a serial acquirer, acquisitions are part of their business, growth strategy and a way to develop their core business* (Wikström, interview 25.11.2011)

In the case of KONE its history of making acquisitions has on its behalf influenced the acquisitions strategy it has today. As literature points out, the corporate strategy of a company is partly a legacy of its past (Porter 1987, 57). The strategy of acquisitions has changed in KONE during its history. From the substantial growth through acquisitions in the past the acquisition strategy has changed to mainly strengthen the core business and the maintenance routes. The acquisitions are often very small, even though KONE also makes regularly some larger acquisitions, and the previous desire to expand and grow internationally or globally has changed more towards strengthening the business and growing market presence in some areas as for example in China. The growth is also limited now, in contrary to the past, by other competitors that have a substantial foothold in the markets, as was pointed out in the analysis of the monopoly theory.

The study opens some issues for further research. The monopoly theory got only vague support in this study, because of the industry the company operates in (Wikström, interview, 25.11.2011). The theory could further be studied in an industry that is not yet taken over by only a few companies. In a setting like this the motive to make acquisi-

tions to achieve monopoly power could be tested more efficiently. The efficiency theory could be confirmed in this study, but to further test the theory it should be analyzed in another industry to see if the operational advantages are as substantial. Further research would also concern the raider theory, empire- building theory, process theory and the disturbance theory. These were not studied in this thesis mainly because of the challenging characteristic of the theories and the difficulty to study them through a case company that would be willing to commit to a study about sensitive issues.

6 SUMMARY

This study investigates the issues that impact the selection of companies a serial acquirer aims to buy. These issues are divided into the study of the acquisition process of a serial acquirer, the motives behind a serial acquirer's interest to acquire companies and the linkage between acquisition strategy and other strategies a company has. Therefore the main research question is: *“What issues impact the selection of acquired companies from the point of view of a serial acquirer?”* This main research question is answered with the help of three sub questions: *“What is a buying process of a serial acquirer like?”*, *“What are the motives for a serial acquirer to buy companies?”* and *“What is the connection between company strategy and serial acquisitions?”*

This study has a qualitative approach to the subject and is conducted through a single case study. The reason why this study was approached through a qualitative perspective was the interest in getting specific and rich information about the subject. The information needed could not have been gathered through a quantitative approach. The use of a single case in this study was partly justified because of the rich information provided from the case and partly because of the lack of time available for conducting the study. The main data source for this study is an interview made with a key person in the case company. The interviewee was chosen because of his specific knowledge of the subject and experience in working with serial acquisitions. Other sources of data used for this study were existing literature and secondary sources for information as company websites and company documents.

The case company KONE selected for this study is a globally operating Finnish company that operates in manufacturing and maintaining elevators, escalators, automatic doors and auto walks. The main reason why this company was chosen for this study was the history it has in making acquisitions, the lack of other similar companies suited for this study and the existing access to the company. KONE has been founded in 1910 and has a long history of making acquisitions. For a long period of time making acquisitions was its main strategy to grow internationally and later globally. The acquisition of some specific companies under its history has boosted the company's internationalization process significantly. KONE as a case company was a clear choice also because of the lack of other similar companies. With similar companies is meant companies that operate globally and can be categorized as serial acquisitions. For the practical part of doing a study it was required that the case company be located in Finland. The last reason for choosing KONE was because of the existing access to the company because of cooperation between the company and the university.

The preliminary framework for this study was created based on the existing literature. Theories about acquisitions and the motives behind them modified the framework. The main research question is partly based on the theory used in the study and partly

based on other literature concerning the topic. The interview questions were based on the theory used in this study and previous literature. The questions are structured according to three of Trautwein's acquisition motive theories and previous literature.

The results from the interview were compared with existing literature and the theories chosen for this study. This way the existing literature and the theories could be tested, confirmed or rejected, against a case company.

The main research findings pointed out that the acquisition process of KONE is compatible with the acquisition process of a successful acquirer recognized in literature. The acquisition process of KONE was compared with a process of a successful acquirer or RAID. The comparison between these revealed that the two processes were compatible. Therefore it can be stated in this study, that the acquisition process of KONE is successful.

The findings supported the efficiency theory in the way that the case company has motives to acquire companies for the benefit for operational synergies. Other synergy advantages, such as financial or managerial could not be discovered. For KONE gaining operational synergies in acquisitions is one of their main motives.

The monopoly theory cannot be supported as widely as the efficiency theory mainly because of the characteristics of the industry the case company operates in. Nevertheless the monopoly theory receives some support, because it may be suggested that making acquisitions due to motives to build monopoly power could be possible in another setting. The restrictions of the industry in this case does not give sufficient support to neither confirm or reject the monopoly theory.

The valuation theory may be rejected in this study. The theory does not get any support from the findings and there are no implications either that the theory would be supported in another setting. The use of private information in the case of KONE was not recognized as a driving force behind making acquisitions. Nevertheless private information was available for the company occasionally, but it was not highly valued. The cases though were private information was possessed, the content of the information was not something that could have been highly valued in an acquisition.

The connection between serial acquisitions and other strategies a company has is obvious. The study suggests strongly that the acquisition strategies are part of company strategy and are also part of the organizational structure. The role of acquisitions can be clearly seen in the organizational structure of the company. The role is equal with other strategic departments. The main strategy for the case company to grow is growing through acquisitions. The other strategy of making acquisitions is to strengthen their maintenance base.

Implications for further research would be studying the acquisition motivation theories in another industry; more specifically the efficiency theory and the monopoly theory. A research conducted in another environment could give quite different results. It

could also be interesting to attempt to further study the other four of the acquisition motive theories; the empire- building theory, the process theory, the raider theory and the disturbance theory.

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APPENDIX 1 INTERVIEW QUESTIONS

Research question 1: What is a buying process for a serial acquirer like?

1. What is the size of the companies you acquire?
 - 1.1. How is their size measured?
2. Because of the density of your acquisitions, it could be assumed that you have overlapping acquisitions. What are the challenges that these overlapping acquisitions bring?
3. Could you describe the acquisition process of your company?
 - How common is it that the process is like this?
4. How long can it take to acquire a company? Assuming that the process starts when the acquired company is chosen and ends to the acquisition agreement.
5. What are the most typical challenges when acquiring companies?
6. How do previous acquisitions affect the future acquisitions?
7. How are the acquired companies chosen?
 - 7.1. Where are the acquired companies found?
 - 7.2. What are the most important criteria?
8. How do you measure the added value an acquired company brings to the acquiring company?
9. How often do acquisitions made by your company fail? Here by failure is meant that the deal is not made.
 - 9.1. Why have the acquisitions failed?

Research question 2: What are the motives for a serial acquirer to buy companies?

10. Who makes the decisions in your company concerning acquisitions?
 - 10.1. Is the decision making process regarding acquisitions decentralized?
11. When are the decisions made about acquired companies?
12. Are there cases, where your company has had more information about the acquired company than the markets? Could you describe a situation like this.
13. What is the most common reason to acquire companies?
14. Have there been acquisitions that have not been profitable? (an acquisition has produced losses/the desired benefits were not reached /the need for the acquisition changed) Could you describe a situation like this.
15. Your company has traditionally made many acquisitions.
 - 15.1. Could you comment on the argument that acquisitions could be made only because of a habit of making acquisitions?
 - 15.2. Acquisition literature suggests that for a serial acquirer the threshold for making acquisitions is small. Can making several acquisitions also complicate the decision making process in an acquisition? For example in a way that past acquisitions may have a negative effect on new acquisitions?

Research question 3: What is the connection between company strategy and serial acquisitions?

16. What is the importance of synergy advantages in your acquisitions?
17. What is the importance of pursuing market area in your acquisitions?
18. How are acquisitions linked to other strategies of your company?
 - 18.1. What is the importance of acquisitions in your growth strategy?
19. How do acquisitions affect the company image?
 - 19.1. Can some companies be bought only to enhance the company image?
20. Have there been acquisitions, that have later on turned out to be a unsuccessful decision for the company strategy? Could you describe an acquisition like this.
21. Has the strategic importance of acquisitions change during the previous five years?
22. Could you describe a situation, where an acquisition has had a significant impact on the company?
23. Are there acquisitions that can be harmful for a company? Could you describe a case like this?
24. How do you see that the acquisition strategy of your company differs from the acquisition strategy of a company that makes rarely acquisitions?