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Employee reactions to M&A: role of LMX and leader communication

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Abstract

Purpose – The purpose of this paper is to assess cognitive, affective, and behavioral reactions of employees to merger and acquisition (M&A) situations.

Design/methodology/approach – The paper reports responses of 225 managers of four banks that have gone through mergers (two merger cases), recently in India. Data are collected on a structured questionnaire containing standard scales of leader-member exchange (LMX), leader communication and employees' reactions to M&As. The psychometric properties of the measures are established before testing the hypotheses.

Findings – Results show that affect mediates the relationship between cognitive and behavioral reactions to M&A. Leader communication fully mediates the relationship of the contribution dimension of LMX with cognitive reactions.

Research limitations/implications – The results have implications for using LMX and communication with the leader in M&A situations. Though, single source data may be a limitation but primary data from real-life M&A situation is strength of the paper.

Originality/value – The study offers insight into the affective, cognitive and behavioral reactions of employees to merger and acquisition situations.

Keywords Acquisitions and mergers, Leaders, Communication, Employee behaviour, India

Paper type Research paper

The uncertainties and ambiguities involved in merger and acquisition (M&A) situations evoke strong psychological reactions from employees. Many researchers (Hunt *et al.*, 1987; Ravenscraft and Scherer, 1987; KPMG, 1997) indicate that about two-thirds of all mergers fail to achieve the desired results primarily because of the organizations' apathy to the employees' reactions and interests (Marks and Mirvis, 1982). Psychological responses of people are shown to have an impact on organizational performance (Cascio and Young, 2003) and, they become more pronounced during situations of drastic change like M&As. The uncertainties of M&A situations trigger a series of psychological processes that result in manifest positive behaviors like commitment and loyalty, or negative behaviors like absenteeism, and sometimes, even acts of sabotage (Bruckman and Peters, 1987; Buono and Bowditch, 1989; Buono *et al.*, 2002; Cartwright and Cooper, 1992, 1993; Cooper and Finkelstein, 2004; Hall and Norburn, 1987; Hubbard and Purcell, 2001; Jemison and Sitkin, 1986; Schuler and Jackson, 2001; Siu *et al.*, 1997).



M&As create a high-anxiety environment which is characterized by uncertainties for employees of the firms (Carey *et al.*, 2004). The impact of this change is seen in the way the employees react. There is a general perception that M&As lead to strong emotional reactions, and little effort is put into segregating the reactions in terms of cognition and affect. Segregating the employee reactions in terms of affect (feelings), cognition (thinking) and behavior helps in not only understanding how emotions and logic link with behavior, but also in identifying appropriate interventions required for handling them. This paper makes several contributions to the existing literature. To begin with, it segregates the employee reactions in terms of cognitive, affective and behavioral reactions to M&As. Understanding these employee reactions and their antecedents helps in identifying the interventions that need to be made to manage the thought processes, the feelings and work behaviors of the employees during M&As. Second, using the role theory and the concept of role ambiguity as the common base for both M&A situations and leader-member exchange (LMX), it highlights the role of LMXs (high and low quality exchanges) in the formation of the employees' reactions to M&As. The two dimensions to LMX – job-related contributions (perceived contribution), and off-the-job interactions (affect) – are expected to predict different employee reactions. The role of communication with the leader is significant, both in M&A situations and in LMX (high- and low-quality leader-member dyads) and, hence, we assess its role as a mediator of LMX and employee reactions relationship. Finally, this study adds to the existing literature, by testing the proposed hypotheses in the Indian context. It should, however, be noted that we are not advocating that the proposed relationships hold true for the Indian context only, they are generalizable to different contexts. However, the results are also discussed in the context of Indian culture.

Theoretical bases and hypotheses development

The human aspect of M&As has long been recognized as a complex process of organizational change (Humpal, 1971). How employees think, feel, and act is important at all times, however, their reactions assume greater significance in times of change like M&As (Buono and Bowditch, 1989). Common reactions discussed in acquisition literature are: anxiety, stress, anger, absenteeism, and lack of involvement in work. While understanding and explaining these reactions, Ivancevich *et al.* (1987) highlight the role of different types of uncertainties claiming that these uncertainties have a significant effect on the organizational members. The first uncertainty, they point out, is the major event that is taking place, which is the merger or the acquisition, over which the employees have little or no control. The second uncertainty which the employees perceive is about their future, as they do not know anything about the objectives of the M&A. Third, they may face changes in jobs, work, and family relationships that would affect their lives, as a consequence of this change. They further point out that each employee cognitively appraises and interprets the situation; thus, a perception of what is happening during the acquisition impacts the employees' response significantly. Consequently, sensitivity to the employee's interests, right from the stage of due diligence, to the eventual merger, makes it easy to achieve the predetermined merger results. Employee reactions to the merger give different signals of what is good and what is not good in the organization, and these are based on employee attitudes towards the merger and/or acquisition situation.

The reported employee reactions involve affective states – changes in the feelings or moods of the employees that occur as a result of M&A and a cognitive appraisal of the situation. Affect is understood as a generic term that includes both strong emotions like fear, anger, and joy; as well as milder feelings and preferences (Pham, 2007). To the best of our knowledge, there is little literature on the cognitive processes that accompany M&As. Cognition involves an appraisal of the situation, using data and information, and developing a mental schema of external reality (Lazarus, 1982). The affective system makes judgmental evaluation and is likely to assign positive and negative valence to the environment, while the cognitive system interprets and makes sense of the world (Norman, 2002). A wide body of literature that exists in social cognitive research examines the relationship/interdependency between cognition, affect and behavior. The extant literature seems inconclusive in advocating the directionality of the relationship between the three constructs (Flint *et al.*, 2005). But it has been found that there is a continuous and pervasive relationship between affect and cognition (Forgas, 1995, 2002; Isen, 2002). It was also observed that cognitive and affective components of attitude are distinctly related to behavior (Breckler and Wiggins, 1989; Miller and Tesser, 1986, 1989; Wilson and Dunn, 1986). Also, affect (Teo *et al.*, 2003) and cognition (Ajzen, 1991) have been shown to predict behavior or behavioral intentions. Hence, we propose our *H1* which concerns the influence of affect and cognition on behavioral reactions to an M&A:

- H1a.* Behavioral reactions of the employees to an M&A will be significantly and positively related to affect such that positive affect would lead to positive behaviors.
- H1b.* Behavioral reactions of the employees to and M&A will be significantly and positively related to cognition such that positive cognition would lead to positive behaviors.

Though affect and cognition are related, there has been much debate on the direction of this relationship. A few believe that affect is independent of cognition while some believe that affect determines cognition (Tomkins, 1981; Zajonc, 1980); still there are others who treat affect as a post-cognitive reaction (Frijda *et al.*, 2000; Lazarus, 1991). The first proposition of affect being independent of cognition, treats cognition as a long drawn process of making sense of the entire reality, based on all possible data. Cognition therefore, is a long-drawn process, whereas, in comparison emotion is a quick affective response to a situation (Zajonc, 1980). However, using Lazarus' (1982) argument, we can say that during inherently ambiguous M&A situations, employees do not always wait for the whole meaning to emerge, instead, they make sense of the small bits and pieces of information. Their emotions emerge as a consequence of this interpretation of data, and they develop concomitant feelings towards the M&A. Changes in affect levels occur as a result of the employee's appraisal of what the event means to him or her. Lazarus (1982, 1984) supports the cognitive-affective model – he suggests that affect depends on cognition which might occur at an unconscious level (Tsal, 1985). The classic two-factor theory (Schachter and Singer, 1964) of emotion suggests that affect is influenced by cognition, in that it provides meaning to undifferentiated emotional arousal. Emotions are intense, complex affective reactions which entail cognitive interpretation of a state of bodily arousal. In his later work, Lazarus (1984, 1991, 1994) gave due importance to the cognitive contribution of affect,

by contending that there is no affect without cognition. This primacy of cognition over affect is the hallmark of work by cognitive behavioral therapists (Beck, 1967; Mahoney and Freeman, 1985; Meichenbaum, 1997). By this argument, cognition precedes affective reactions, in the light of this, we propose our next hypothesis:

- H2.* Affective reactions mediate the relationship between cognitive and behavioral reactions to M&As.

We now look at how immediate leaders help in the formation of affective and cognitive reactions in M&A situations.

LMX and reactions to M&As

Many studies have emphasized the importance and significance of the leader's personality and behavior in helping the employees cope with M&As (Cartwright and Cooper, 2000; Haspeslagh and Jemison, 1991; Marks and Mirvis, 2001). Though most of the studies have focused on the role of the top management (the chief executive officer) in clarifying the M&A goals and strategy well in time, the immediate leaders also play a significant role in helping employees cope with the changes and their concomitant reactions to M&As. Immediate leaders become important as they provide relevant information and thus become the subordinates' interface with the organization. The amount and quality of information that the subordinates get on the M&A is dependant on the exchange relationship between the leader and the individual subordinate. LMX has been defined as the quality of exchange relationship between the supervisor and each of his or her subordinates (Dienesch and Liden, 1986). Leaders are shown to develop different qualities of work relationships with different subordinates (Graen and Scandura, 1987; Scandura and Graen, 1984; Scandura and Schriesheim, 1994). High-LMX members enjoy high-exchange quality relationship which is characterized by liking, loyalty, professional respect, and contributory behavior (Dienesch and Liden, 1986; Liden and Maslyn, 1998). The out-group (low LMX) members, on the other hand, are deprived of all these. Most of the earlier conceptualizations of LMX have treated it as a one-dimensional construct in predicting subordinate-related outcomes. In this one-dimensional measurement, the exchange or the quality of interaction in a leader-member dyad is limited to the job and tasks at hand, with little or no focus on social interactions.

Development of varying qualities of interactions in a leader-member dyad has been understood in terms of role development and social exchanges (Graen and Scandura, 1987). The leader assesses the competencies and motivation of the subordinates through role making episodes and offers different inducements to different subordinates depending on their ability and motivation to collaborate on unstructured tasks. How a subordinate defines the role determines the quality of interaction in a leader member dyad. According to the role theory (Jacobs, 1971; Katz and Kahn, 1978), roles are multidimensional and are likely to have different combinations of task focus and social interaction (Bales, 1958). Further, the nature of interaction in different quality dyads is maintained through social exchanges. These exchanges are also conceptualized as multidimensional, involving material and non-material rewards like advice, workflow, and friendship. Since both roles and exchanges are multidimensional, Dienesch and Liden (1986) and Liden and Maslyn (1998) propose that LMX too, needs to be studied as a multidimensional construct.

Dienesch and Liden (1986) suggested that LMX may be based on three “currencies” of exchange: task behaviors (perceived contribution), loyalty to each other (loyalty), and liking for each other (affect). Perceived contribution deals with on the job dimension of interactions, loyalty deals with social support, and affect deals with affective feelings of liking which go beyond the work situation. This conceptualization was subsequently used by researchers to develop psychometrically sound scales of LMX (Bhal and Ansari, 1996; Liden and Maslyn, 1998). The Bhal and Ansari (1996) study resulted in a two-dimensional scale consisting of two orthogonal dimensions: LMX-contribution and LMX-affect. The two dimensions of contribution and affect which relate to on-the-job, work-related formal interactions and off-the-job, informal interactions, respectively, are in line with the previous two dimensions of leader behavior, which have viewed leader behavior as consisting of consideration and initiating structure (Halpin and Winer, 1957), concern for people and concern for production, (Katz and Kahn, 1978), and employee orientation and production orientation (Blake and Mouton, 1964). Maslyn and Uhl-Bien (2001) are of the view that the affect, loyalty, and professional respect dimensions are more like social currencies that focus on the social exchange between the leader and the member, whereas the contribution dimension is more like a work-related currency. They included socially related currencies on the ground that exchange between the leader and the members is not based only on work-related elements (Bhal and Ansari, 1996; Liden *et al.*, 1997). Thus, a high “contribution-dominated” exchange (work-related currency) is likely to involve intensive interaction on task-related activities, whereas an “affect-dominated” exchange (social currency) is likely to involve off-the-job, affective, and personal interactions. The basis of development of different qualities of exchange, as mentioned earlier, lies in the role development process, which helps employees in clearing any ambiguities in their roles and seeking clarity on their jobs.

In situations that have role ambiguity and require organizational members to clarify and define their roles, the role of the LMX is likely to be enhanced. M&A situations are characterized by high uncertainties and high ambiguities in the job (Marks, 1988, 1999; Marks and Mirvis, 1986). LMX is the leader’s mechanism of helping the subordinates clarify and develop their role definitions. Hence, during the drastic changes of an M&A, the immediate leader helps the subordinates develop their roles. During this time, what the employees require are on-the job information and clarifications from the leader. The leader’s contribution to the subordinate’s job becomes very significant because it helps the subordinates form appropriate cognitions. By helping the subordinates on personal, off-the-job issues, the leader helps reduce negative affect (Seo *et al.*, 2007). Thus, our next hypothesis is as follows:

H3a. Employees’ cognitive reactions to M&As are predicted by the contribution (of the leader as perceived by the subordinates) dimension of LMX.

It might be argued that affective reactions to an M&A situation might be guided by affect for the leader as the manager’s affective behaviors directly influences the subordinates’ affective experience. However, in situations of an M&A, negative affect largely emanates from uncertainties on the job and the subordinates require job-related clarifications to alleviate the anxieties related to the M&A. Thus, focusing only on affective relations between the leader and the member may not provide full explanation

of the employee's affective reactions to the M&A; the contribution dimension also becomes significant. Consequently, we propose the following hypothesis:

- H3b.* Employees' affective reactions to M&As are predicted by both contribution and affect (of the leader, as perceived by the subordinates) dimensions of LMX.

LMX – reactions to an M&A relationship: the role of communication

An M&A is characterized by drastic changes, and lack of communication during an M&A situation, is one of the most cited reasons for M&A failures (Cartwright and Cooper, 1992; Huy, 1999). During such times of radical changes, employee reactions of stress, fear, and anxiety are mostly attributed to lack of information. Bastien (1987) analyzed interview data from 21 managers of three different organizations, and concluded that communication has the potential to increase performance, and reduce uncertainty. The studies by Napier *et al.* (1989) and Graves (1981) also concluded with similar results, and suggestions for increased communication between the employees and the organization. Most of the studies on M&As focus on organizational communication processes in terms of announcements, newsletters and other organization wide mechanisms of disseminating information (Schweiger and DeNisi, 1991). The immediate leader, who is the most immediate representative of the organization is the carrier of valuable organizational information. Thus, communication with the immediate leader acquires a greater significance during M&A situations.

The need for knowledge and information sharing is higher than usual during times of radical change like M&As, and employees try to make sense of the new reality through the data and information that they have with them. Research has shown that high-LMX relationships, besides being characterized by trust and latitude, also show higher levels of positive and supportive communication (Maslyn and Uhl-Bien, 2001) and poor quality relationships are characterized by dominance-like, restricted communication (Fairhurst *et al.*, 1987). Given the significance of communication in the M&A process, we believe that it is the quality and quantity of communication between the leader and subordinates that is the underlying mechanism through which LMX improves the reactions of employees to M&A situations. In other words, subordinates having high-quality interactions with their leaders are likely to have positive affective, cognitive and behavioral reactions to M&As situations because of better communication. Consequently, we propose the following hypothesis:

- H4a.* The relationship of perceived contribution aspect of LMX with the affective responses of employees during M&As is mediated by communication with the leader.
- H4b.* The relationship of perceived contribution aspect of LMX with the cognitive responses of employees during M&As is mediated by communication with the leader.
- H4c.* The relationship of perceived contribution aspect of LMX with the behavioral responses of employees during M&As is mediated by communication with the leader.

Employee reactions have an impact on overall performance of the organization, we propose to compare the affective, behavioral, and cognitive reactions to M&As for different mergers. The mergers that show better performance indicators (post merger) are likely to show more positive affective, cognitive, and behavioral reactions to M&As.

Methodology

The study was conducted in two cases of bank-mergers in India. These mergers were included in the study as they had occurred within the last two years (at the time of data collection). The two year criterion for selecting sample organizations is important because employees' reactions and communication mechanisms are generally more pronounced during the first two years of the M&A, after which they settle down. For homogeneity in the sample organizations, only mergers in the banking industry were selected for the study. The site for this research was four banks that had gone through M&A. Two banks (one was a public sector bank with the government as the owner, 1A and the other under the private sector, 1B) were involved in Merger 1. The two other banks, 2A and 2B, involved in Merger 2 were from the private sector. They were situated in the Indian States of Punjab, Delhi, Andhra Pradesh, Maharashtra, Orissa, and the National Capital Region of Delhi. For the sake of making the sample representative for the study, effort was made to cover those cities which had the maximum number of branches of the merging banks. The details of the four organizations involved in the merger are given in Appendices 1 and 2.

Sample and procedure

Full-time employees working in the four banks undergoing merger constituted the sample for the research. Their responses were sought on a structured questionnaire.

Sample respondents. This study was conducted on the executives working in the merged banks during the period March 2006-January 2007. The questionnaires were personally distributed (by the second author) to 406 executives, by making several visits to the sample organizations. The completed questionnaires were collected personally from the respondents. Only 13 questionnaires were received through mail. The final sample constituted 225 executives from the four merging bank partners. The response rate of Merger 1 was 51 percent, and that of Merger 2 was 60.8 percent. The response rate of 2B was the highest among all the merger partners (70.2 percent) and the response rate of 1A was the lowest among all the merger partners (48 percent). The sample consisted of 51 (22.7 percent) and 70 (30.7 percent) respondents from organizations 1A and 1B; and 52 (23.1 percent) each from organizations 2A and 2B.

The total number of respondents who did not respond to the survey was 181. Out of that, 127 (males = 113 and females = 14) were from Merger 1 and 54 (males = 48 and females = 6) were from Merger 2. The average age of the non-respondents was 37.9 years (SD of 9.22). About 37 non-respondents were from senior management positions, 62 were from the middle level and 82 were from the lower level management. In total, 21.47 percent of the respondents initially contacted were from the top management; 36.59 percent were from the middle level and 41.95 percent were from the lower level. A χ^2 -test was done to compare the non-response pattern across the levels; the expected frequencies were based on the total number of respondents initially

contacted at each level. χ^2 -value was 0.85 ($p > 0.65$), which was not significant. The results showed that there was no systematic non-response bias across different levels.

The respondents were asked not to mention their names and they were assured of confidentiality of the data. Their average age was 34.40 years (SD of 8.97 years) and average the experience was 6.44 years (SD of 5.44 years). Of the 225, 174 (77.3 percent) were male and 51 (22.7 percent) were female respondents. There were no lay-offs in both the merger cases except that some employees of organization 1B quit the merged entity soon after the merger. There were job changes/changes in profiles in case of 80 percent of the respondents, 30 percent had new superiors/supervisors. About 47 respondents were occupying senior management positions, 88 were from the middle management level and 90 were from the lower management cadre.

Measures

Standard questionnaires were used to collect data, since all working managers had a good knowledge of English; there was no need to translate the questionnaires.

LMX-perceived contribution and affect. LMX was assessed using a ten-item scale by Bhal and Ansari (1996). They developed a two-dimensional scale of LMX, based on the conceptualization given by Dienesch and Liden (1986). The two dimensions were contribution and affect. The scale consisted of ten items, with five items each of perceived contribution and affect. The respondents were asked to rate the statements on a seven-point scale (1 – not at all; 7 – very much), as to how true were the statements, for their relationship with their supervisor. Some items for perceived contribution are “How much responsibility does he/she take for the jobs that are to be done jointly by him or her?” and “How efficient is his/her contribution on the jobs for which the two of you work together?” The scale’s reliability assessed through Cronbach’s coefficient alpha in this study was 0.93.

Affect dimension measures the quality of the interaction between the superior and the subordinate in terms of mutual liking, seeking advice on personal matters, taking help in personal matters, etc. Example items are “How much importance do you attach to each other’s advice on personal matters?” and “How much do you help each other in personal matters?” The scale’s reliability assessed through Cronbach’s coefficient alpha in this study was 0.86.

Leader communication. Two-items from Roberts and O’Reilly (1974) were used to measure the level of communication with the leader. The two items are “I get accurate information from my superior” and “I discuss job related problems with my immediate superior.” The respondents were asked to rate each item on a nine-point scale (1 – strongly disagree; 7 – strongly agree) as used in the original study. The scale’s reliability assessed through Cronbach’s coefficient alpha in this study was 0.69.

Affective, cognitive and behavioral reactions to merger. Oreg (2003) had used a scale to assess reactions to change. We modified the scale to capture reactions towards the mergers that had taken place in the study organizations. The items from this scale were grouped into affective, cognitive and behavioral reactions. The respondents were asked to rate each item on a six-point scale (1 – strongly disagree; 6 – strongly agree) as in the original scale.

Six items from the scale were classified as affective reactions. They are as follows: “This whole merger makes me kind of angry” (reverse coded); “I am emotionally overwhelmed by all the things that need to be done because of the merger”

(reverse coded); "I'm excited about the merger" "I'm really sad we have merged" (reverse coded); "I try not to think about the merger because when I do, I get too stressed out" (reverse coded); and "I'm worried about what things will be like in the future" (reverse coded). The scale's reliability assessed through Cronbach's coefficient alpha in this study is 0.79.

Three items from Oreg (2003) were classified as cognitive reactions. These items seek the respondents' opinion about the necessity of the merger, comparing the merger situation with the earlier situation, and the goodness of the merger. The items are "I think I am better off after the merger, as compared to my situation before the merger," "I think the merger will do us all good," and "I think it is good that we're going through this merger." The scale's reliability assessed through Cronbach's coefficient alpha in this study is 0.814.

Three items from Oreg (2003) were grouped as behavioral reactions to a merger. The items are as follows: "I find that I'm not as efficient or productive as usual these days" and due to the merger, "I tend to be very distracted and inefficient at work these days," "During these days of the merger I find it particularly difficult to motivate myself to do the things I know I should". All the three items were reverse coded. The scale's reliability assessed through Cronbach's coefficient alpha in this study is 0.74.

Results

The scales on LMX and leader communication were established scales. The reactions (affective, behavioral, and cognitive) to M&A scale was modified for use in M&A situation. Consequently, we checked the construct validity of reactions to M&A, using confirmatory factor analysis (CFA). Using Amos 5.0, the fit of a CFA model to the observed data were evaluated to determine if the items loaded on their respective dimensions (affective, behavioral, and cognitive reactions). Four measures were used to assess the fit of structural models: the goodness-of-fit index (GFI), the adjusted goodness-of-fit index (AGFI) (Joreskog and Sorbom, 1993), comparative fit index (CFI) given by Bentler (1990), root mean square error of approximation (RMSEA) (Browne and Cudeck, 1989), and normed fit index (NFI).

For CFA of the scale, first a single-factor model was estimated. This model provided poor fit to the data ($\chi^2 = 516.067$, $df = 54$, $GFI = 0.632$, $AGFI = 0.469$, $CFI = 0.665$, $RMSEA = 0.195$, $NFI = 0.642$). Then, we tested a three-factor (hypothesized) model against a single-factor model. The three-factor model showed superior results (fit indices) than the one factor model. The fit indices to the three-factor model are ($\chi^2 = 345.841$, $df = 51$, $GFI = 0.769$, $AGFI = 0.647$, $CFI = 0.786$, $RMSEA = 0.161$, $NFI = 0.760$). Three factor model shows much improved fit indices in comparison to the one-factor model. All the items were significant predictors of their respective latent variables.

The reliability of the scales was assessed through Cronbach's coefficients alpha. The reliability coefficients and inter correlations among the study variables are contained in Table I. Table I shows that reliabilities of the study variables range from 0.69 to 0.91, which is acceptable (Hair *et al.*, 1998). In conclusion, the results of reliability coefficients indicate that the measures have sound psychometric properties.

After confirming the factor structure of the reactions to M&A scale and reliabilities of all the scales, we formed composite variables for each construct from their respective items and used those composites as single predictors of their respective factors.

Almost all the correlations among study variables are in the expected direction. Strong and significant correlations among the affective cognitive and behavioral reactions to M&As provide full support to our *H1a*. Lack of significant correlation between the affect dimension of LMX and affective reactions to M&As does not support *H1b*.

Since gender is shown to be important in affective (Mathieu and Zajac, 1990; Mowday *et al.*, 1982), and cognitive (Venkatesh *et al.*, 2000) reactions of employees in the workplace, we wanted to rule out its effect; hence gender was added as an independent variable in all the regression equations.

To test *H3a*, cognitive reactions to M&A were regressed on gender, perceived contribution and affect dimensions of LMX using a simultaneous entry method. This method enables one to ascertain whether a dimension of LMX helped explain variance in cognitive reactions (dependent variable) after accounting for the effects on the other dimension. For cognitive reactions to M&A (*H3a*), the model was significant at 0.000 level ($R^2 = 0.174$). β -coefficient for perceived contribution was 0.46 ($t = 6.21$, $p < 0.000$). However, the β -coefficient for affect was -0.09 ($t = -1.15$, $p < 0.251$). In line with *H3a*, perceived contribution had a significant positive impact on cognitive reactions to M&As. Since zero-order correlations between leader affect and affective reactions to M&A are not significant (Table I), our *H3b* does not find support from the data.

H2, *H4a*, *H4b* and *H4c* are mediation hypotheses. To test these hypotheses, the three conditions of mediation proposed by Baron and Kenny (1986) were assessed, the:

- (1) predictor (independent variable) must significantly impact the mediator;
- (2) predictor must significantly impact the criterion (dependent variable); and
- (3) mediator must impact the criterion variable and the impact of predictor (independent variable) on criterion must either become insignificant (total mediation) or must become less significant (partial mediation) when the criterion is regressed on both independent and mediator variables in the third condition.

H2 predicted that the relationship between cognitive and behavioral reactions to M&As would be mediated by affective reactions. Table II reports the result of regression analysis for *H2*, i.e. affective reactions mediate the relationship between cognitive and behavioral reactions to M&A. The results are also shown in Figure 1.

	Mean	SD	1	2	3	4	5	6
1. LMX-PC	5.22	1.43	0.93					
2. LMX-Af	3.73	1.43	0.56**	0.86				
3. Affective RMA	4.13	1.29	0.27**	-0.01	0.79			
4. Cognitive RMA	3.61	1.44	0.41**	0.17*	0.73**	0.81		
5. Behavioral RMA	4.91	1.22	0.204**	-0.06	0.56**	0.32**	0.74	
6. Leader communication	5.31	1.71	0.76**	0.38**	0.28**	0.44**	0.25*	0.69

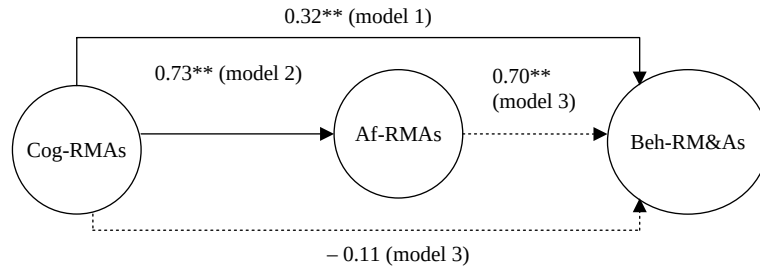
Notes: Correlation is significant at: *0.05 and **0.01 levels (two-tailed), respectively; $N = 225$; numbers along the diagonal indicate the reliability coefficients; LMX-PC – leader member exchange-perceived contribution, LMX-Af – leader member exchange-affect, RMA – reactions to mergers and acquisitions

Table I.
Means, standard
deviations, Cronbach's
coefficients alpha, and
correlations among study
variables

Table II.
Regression results:
affective reactions to
M&A as a mediator of
cognitive and behavioral
reactions (*H2*)

Criterion	Predictor(s)	Unstandardized β	Standardized β	R^2	F	df
<i>Model 1</i>						
Beh-RMA	Gender	0.41 ^{*1}	0.14	0.124	15.720 ^{**}	2.222
	Cognitive-RMA	0.27 ^{**2}	0.32			
<i>Model 2</i>						
Affective-RMA	Gender	0.02 ¹	−0.01	0.540	130.165 ^{**}	2.222
	Cognitive-RMA	0.61 ^{*2}	0.73			
<i>Model 3</i>						
Cog-RMA	Gender	0.43 ^{*1}	0.14	0.353	402.204 ^{**}	3.221
	Cognitive-RMA	−0.17 ²	−0.20			
	Affective-RMA	0.63 ^{*3}	0.66			

Notes: ^{*} $p < 0.05$, ^{**} $p < 0.001$; Model 1 – predictor predicts the criterion, Model 2 – predictor predicts the mediator, Model 3 – both predictor and mediators predict the criterion; MS – model summary



Notes: LMX- PC = LMX-perceived contribution; lead comm = leader communication; Cog M&As = cognitive reactions to M&As; ^{**} $p < 0.01$

Results in Table II and Figure 1 show that though cognitive reactions predict both behavioral and affective reactions to an M&A independently, once both cognitive and affective reactions are allowed to jointly predict behavioral reactions, the impact of cognitive reactions becomes insignificant indicating a full mediation by affective reactions. Thus, *H2* finds full support from the data.

As mentioned earlier, *H4a*, *H4b* and *H4c* are mediation hypotheses predicting leader communication as the predictor of LMX and M&A reactions relationship.

Results in Tables III-V show that communication with the leader mediates the relationship between LMX and the cognitive reactions to an M&A (Figure 2).

Thus, our *H3b* finds support from the data as the relationship of LMX with cognitive reactions to M&As only gets mediated by communication with the leader. The two other relationships of LMX with affective and behavioral reactions do not get mediated by communication, and our *H3a* and *H3c* do not get supported by the data.

Finally, we compared the affective, behavioral and cognitive reactions to M&As for the two mergers under study. Independent samples *t*-test was conducted to compare these reactions to two mergers; results are reported in Table VI. It can be seen that people in Merger 2 shows significantly more positive affective, behavioral and cognitive reactions to M&A as compared to people in Merger 1.

The results are in sync with the performance of the two mergers (Appendices 1 and 2).

Criterion	Predictor(s)	Unstandardized β	Standardized β	R^2	F	df
<i>Model 1</i>						
Af-RMA	Gender	0.02 ¹	0.01	0.075	9.02 ^{**}	2.222
	LMX-PC	0.23 ^{**2}	0.27			
<i>Model 2</i>						
L Com	Gender	0.83 ^{**}	0.20	0.62	180.39 ^{**}	2.222
	LMX-PC	0.91 ^{**}	0.76			
<i>Model 3</i>						
Af-RMA	Gender	0.14	-0.05	0.09	7.34 ^{**}	3.221
	LMX-PC	0.10 ²	0.12			
	L Com	0.14 ³	0.20			

Notes: * $p < 0.05$, ** $p < 0.001$; Model 1 – predictor predicts the criterion, Model 2 – predictor predicts the mediator, Model 3 – both predictor and mediators predict the criterion; MS – model summary

Table III.
Regression results: leader communication as a mediator of LMX and affective reactions to M&As

Criterion	Predictor(s)	Unstandardized β	Standardized β	R^2	F	df
<i>Model 1</i>						
Cog-RMA	Gender	0.001 ¹	0.00	0.17	22.628 ^{**}	2.222
	LMX-PC	0.42 ^{**2}	0.41			
<i>Model 2</i>						
L Com	Gender	0.83 ^{**}	0.20	0.62	180.39 ^{**}	2.222
	LMX-PC	0.91 ^{**}	0.76			
<i>Model 3</i>						
Cog-RMA	Gender	-0.23 ¹	-0.07	0.21	19.81 ^{**}	3.221
	LMX-PC	0.16 ²	0.16			
	L Com	0.28 ^{**3}	0.34			

Notes: * $p < 0.05$, ** $p < 0.001$; Model 1 – predictor predicts the criterion, Model 2 – predictor predicts the mediator, Model 3 – both predictor and mediators predict the criterion; MS – model summary

Table IV.
Regression results: leader communication as a mediator of LMX and cognitive reactions to M&A

Criterion	Predictor(s)	Unstandardized β	Standardized β	R^2	F	df
<i>Model 1</i>						
Beh-RMA	Gender	0.41 ^{*1}	0.14	0.06	7.22 ^{**}	2.222
	LMX-PC	0.17 ^{**2}	0.20			
<i>Model 2</i>						
L Com	Gender	0.83 ^{***}	0.20	0.62	180.39 ^{***}	2.222
	LMX-PC	0.91 ^{***}	0.76			
<i>Model 3</i>						
Beh-RMA	Gender	0.30	0.10	0.07	5.81	3.221
	LMX-PC	0.05	0.07			
	L Com	0.13	0.18			

Notes: ** $p < 0.05$, *** $p < 0.001$; Model 1 – predictor predicts the criterion, Model 2 – predictor predicts the mediator, Model 3 – both predictor and mediators predict the criterion; MS – model summary

Table V.
Regression results: leader communication as a mediator of LMX and behavioral reactions to M&A

Discussion

The study was designed to examine the affective, cognitive and behavioral reactions of the employees to M&A situations. The site and the timing of the study were carefully chosen for the reactions to mergers to become manifest and salient. The study presents the results of two bank mergers and the data were collected after six months of the merger to capture the employee reactions in a post merger scenario. Specifically, it was designed to assess:

- the link among the three types of reactions to M&As;
- their relationship with LMX; and
- the mediating role of communication in the relationship.

Results show several interesting trends. First, our *H3b* does not find support from the data, and the affective dimension of the LMX shows no correlation with affective reactions to M&As, signifying the lack of its importance in forming reactions to M&As. We had conceptualized LMX-affect as off-the-job interactions on personal (non-job related) issues. M&As are characterized by extreme emotional reactions but these reactions stem from on-the-job situations that in turn are characterized by extreme ambiguities and uncertainties. In these situations, it is likely that personal, off-the-job interactions do not help in alleviating the anxieties and emotional reactions stemming from on-the-job issues, and thus, these interactions become insignificant. To some extent, this result supports the contention that emotions in M&As cannot be managed by affective relations with the boss as they require on the job cognitive

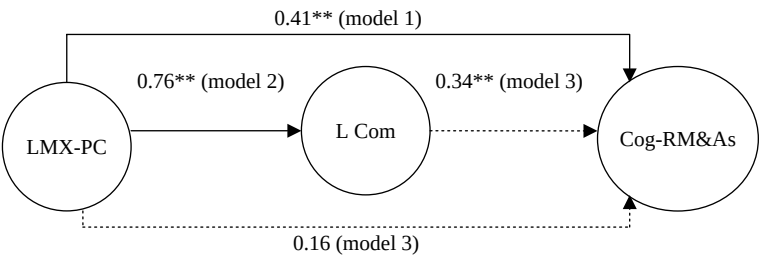


Figure 2.
Standardized regression
coefficients for direct and
mediation equations (*H4b*)

Notes: LMX- PC = LMX-perceived contribution; lead comm = leader communication; Cog M&As = cognitive reactions to M&As; ***p* < 0.01.

Table VI.
t-test for comparing
affective, behavioral, and
cognitive reactions in the
two merger cases

	Merger	<i>n</i>	Mean	SD	<i>t</i>
Cognitive reactions to M&A	1.00	118	3.2034	1.39	− 4.65 *
	2.00	107	4.0592	1.36	
Affective reactions to M&A	1.00	118	3.7006	1.21	− 7.12 *
	2.00	107	4.7259	0.94	
Behavioral reactions to M&A	1.00	118	4.4520	1.35	− 6.608 *
	2.00	107	5.4174	0.79	

Note: **p* < 0.001

information (Frijda *et al.*, 2000). The primacy of perceived contribution in reactions to M&As further supports this contention.

Second, leader communication mediates the relationship between perceived contribution and cognitive reactions to M&As, whereas, it does not mediate relationships with affective and behavioral reactions. Perceived contribution involves an active assessment of issues at work, Graen and Uhl-Bien (1995, pp. 237-8) have commented:

Development of LMX is based on the characteristics of the working relationship as opposed to a personal or friendship relationship, and this trust, respect, and mutual obligation refers specifically to individual assessments of each other, in terms of their professional capabilities and behavior.

The evaluation process can be considered predominantly cognitive. Moreover, merger situations are characterized by knowledge gaps, wherein employees of the two firms do not have enough knowledge about each other. Yoo *et al.* (2007) highlight the role of knowledge sharing in a post merger scenario. The immediate leader, through job-based communications, becomes the mechanism of knowledge sharing during such times, which helps in the sense making process during ambiguities of M&A situations. During such times, employees clearly perceive a need for informative communication which helps them cognitively appraise the situation (Haspeslagh and Jemison, 1991).

Cognitive reactions emerge as important in M&A situations. Researchers have identified the “merger syndrome” which is characterized by intense emotions like fear, insecurity, anxiety, and the like (Appelbaum *et al.*, 2000a, b; Marks and Mirvis, 1986). However, as these emotions are rooted in cognitive appraisals of the situation, the root to dealing with employee reactions is cognitive which needs to employ the mechanisms of informative communication. Our results support the cognitive appraisal view of emotions (Cornelius, 1996; Parkinson, 1997). As mentioned earlier, Schachter and Singer (1964) first proposed that the interpretation of a situation is important for the full experience of emotions. Subsequently, all cognitive appraisal theorists recognize that cognitive evaluation of the situation precedes emotional response.

Finally, our results of comparison between the two merger cases show that merger situation where proactive measures are taken and which show positive results (as mentioned in Appendices 1 and 2) are supported by positive affective, behavioral, and cognitive reactions.

Practical considerations

The study has practical relevance for practicing managers as well. Given the power of emotional responses during M&A situations, those who are managing people are likely to get overwhelmed and impressed by the emotions and devise mechanisms to deal with the emotions to manage reactions to M&As. Our study, however, highlights the significance of cognition in reactions to M&As. This provides support for a rational basis of emotions and allows individuals and organizations to deal with emotions rationally, by addressing the cognitive issues.

One of the cognitive mechanisms to deal with reactions to M&As seems to be communication by the leader. Organizations are known to hold back information and know-how during these times (Marks, 1999) though they might use some supportive mechanisms superficially. Our results however show that though emotions are strong they need to be handled at the cognitive level and employees need to be provided

communication that is informative (not merely supportive, in response to emotional reactions).

The results have implications for LMX enhancement interventions. In general, enhancing work-related interactions through guiding, sharing, and communicating (Bauer and Green, 1996) can result in positive employee reactions to M&As. Leaders also need to be trained to develop skills for providing informative communication to all the employees.

Limitations and future research

The implications of the study must be considered in the light of its limitations. First, all the data for this study was collected from a single source, raising concerns of the common method bias. However, we conducted a CFA of all the scales used, which provided evidence for independence of scales. Second, since the data were cross-sectional, the direction of causality is assumed, not tested. Thus, inclusion of longitudinal studies and other ratings of behavior and attitudes could provide support for the current findings. Third, all the data have been collected through self-reports, which may be limited. However, recent research suggests that self-reported data are not as limited as was previously believed and that people often perceive their social environment accurately (Alper *et al.*, 1998). Further, self-reports are also likely to be influenced by social desirability. Although this bias cannot be ruled out, some researches have shown that social desirability may not be a source of bias in measuring organizational perceptions (Moorman and Podsakoff, 1992; Spector, 1987). Finally, we recognize that there are some individual level factors that might result in different reactions but we have not included these variables in our study. Future studies might incorporate these factors, while assessing reactions to M&As.

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Appendix 1. Organizational details of Merger 1

Organization 1A

It was established in Lahore (Pakistan) in 1943. After partition, the bank shifted its Registered Office from Lahore to a place in Punjab and in 1950 to Delhi (the national capital). This bank was nationalized on April 15, 1980. It has a high-capital adequacy ratio, one of the lowest non-performing assets, and one of the highest productivity ratio, per employee. At the time of the merger, it had a network of 530 branches spread throughout India, out of which 490 branches offered centralized banking solutions. It also had a network of 505 ATMs.

The bank has been rated "AAA" by the leading rating agency, ICRA. In 2003, it was declared as the "Best under a billion" by the *Forbes Global 200* best small companies for 2003. At the time of the merger, the employee strength was 14,730.

Organization 1B

Established in 1993 and headquartered at Secunderabad, it was promoted as a private sector bank by three promoters, against the backdrop of the government's policy of deregulation and liberalisation. It was once touted to be one of India's best, before it succumbed to staggering non-performing assets. The bank had a network of 104 branches and 275 ATMs in 34 cities across the country. The bank had been running its operations successfully (Rs. 11.8 crores in net profits for the nine-month period ending December 31, 2003) and setting records until it collapsed under the pressure of bad loans. At the time of the merger, it had an employee strength of 2,204.

Post-merger performance

The first year profits post merger (2004-2005) were affected because of writing-off 61,240 million liabilities on account of the amalgamation of 1B with 1A. But 2005-2006 saw a jump of 37.2 percent in profit after tax at 310,750 million *vis-à-vis* 226,510 million for the previous year. Business volumes have also grown, but the exact figures could not be obtained. The merged entity has also opened some new branches. Post merger 60 percent of the erstwhile 1A employees have resigned from the merged entity. The new merged entity was running short of personnel to conduct business at the erstwhile 1A branches.

Appendix 2. Organizational details of Merger 2

Organization 2A

This bank became operational from April 1995, when its first branch was opened in Chandigarh. By March 1996, its deposit base was Rs 2,342.17 crores. In four years, the annual growth rose to Rs 3,244.76, which was 200 percent. It was the first bank to focus on retail banking and to introduce faxbanking and telebanking for its customers. It has a strong presence in Punjab,

Haryana, Delhi, and other parts of North India. However, at the time of merger this bank was not performing too well. At the time of the merger, the employee strength of this bank was 2,014.

Organization 2B

The bank was incorporated on June 30, 1994, under an overall economic reform program initiated by the Government of India in 1991. It was started by a non-resident Indian along with Keppel Tatlee Bank Limited (which was earlier the Keppel Bank of Singapore) through Kephinance Investment (Mauritius) Pte. Limited. Besides, the then promoters, the Equity Share capital was subscribed by ADB, Manila and IFC, Washington. It was among the first banks to enter the profitable two-wheeler, commercial vehicles, and construction equipment financing businesses. As on March 31, 2004, it had a network of 61 fully networked branches covering 45 cities, 148 ATMs, 20 extension counters, and 23 marketing offices. It has a pan-India presence, with a strong presence in Southern and Western India. At the time of the merger, the employee strength was 1,913.

Post-merger performance

Both the merger partners (2A and 2B) were incurring losses individually. In the first year after the merger, the merged entity earned profits of 800 million. Net profits for the fiscal year 2006-2007 were 1,210 million. This is a 38 percent rise as compared to the previous year. Operating profit grew 144 percent over the same period. The entity has reported the highest net interest margins in the industry at 4.6 percent. The business volume has grown as well as the number of branches. Employee count has also increased by 50 percent after the merger. Both the merger partners (2A and 2B) were incurring losses individually. In the first year after the merger, the merged entity earned profits of 800 million. Net profits for the fiscal year 2006-2007 were 1,210 million. This is a 38 percent rise as compared to the previous year. Operating profit grew 144 percent over the same period. The entity has reported the highest net interest margins in the industry at 4.6 percent. The business volume has grown as well as the number of branches. Employee count has also increased by 50 percent after the merger. Compared to the pre-merger performance of the two banks, post merger performance of this merger is very good.

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