Work-in-progress paper submitted to the 31st Annual IMP Conference

Corporate Acquisitions and Reactivation of Business Relationships: The importance of relationship infrastructure

Anna Bengtson, Mikael Gidhagen, Virpi Havila[1], León Poblete
Uppsala University, Department of Business Studies, Sweden

Abstract

In literature dealing with corporate acquisitions, the implicit assumption is that through an acquisition a company can get access also to the target company's ongoing customer and supplier relationships. However, earlier research has shown that business relationships can deteriorate and even be terminated as a consequence of a corporate acquisition (e.g. Anderson, Havila and Salmi, 2001). Thus, corporate acquisitions may have a negative influence on the target company's ongoing customer and supplier relationships (Holtström, 2009; Öberg, 2008).

In this paper our purpose is to elaborate on the opposite situation, that is, when an acquisition has positive effects on the target company's business relationships, in that e.g. former relationships are reactivated after an acquisition. In our argumentation, special attention will be given to the impact of embeddedness, or as we term it in the paper: relationship infrastructure. Only few studies are found that focus on reactivation of business relationships (see Polonsky et al., 2010 and Leach & Liu, 2014), hence we still know little about the reactivation process and how it is affected by its context. The herein contended discussion is based on two ongoing case studies of reactivation of business relationships after a corporate acquisition. The first case deals with a situation when a former employee acquires a company following bankruptcy and how a previously terminated customer relationship is reactivated. The second case, in turn, deals with a situation when a newly established company decides to reopen a mining field, reactivating relationships that were terminated 20 years earlier.

The case studies indicate that corporate acquisitions may lead to radical changes in business networks. Whereas earlier findings show termination effects, we maintain that reactivation effects dealing with the impact of the existing or non-existing relationhip are contingent on relationship infrastructure.

[1] Corresponding author: Virpi Havila (virpi.havila@fek.uu.se), Uppsala University, Department of Business studies, P.O. Box 513, SE-751 20 UPPSALA, Sweden. Tel. +46 18 471 1615.

Corporate Acquisitions and Reactivation of Business Relationships: The importance of relationship infrastructure

1. Introduction

In literature dealing with corporate acquisitions, the implicit assumption is that through an acquisition a company can get access also to the target company's customer and supplier relationships (Anderson, Havila and Salmi, 2001). However, earlier research has shown that corporate acquisitions can cause disturbance in the target company's ongoing customer and supplier relationships (Holtström, 2009; Öberg, 2008). The disturbance may have a negative influence on the relationships. For example, some of the business relationships can deteriorate and even be terminated as a consequence of a corporate acquisition (Ibid.). There are nevertheless indications of that corporate acquisition may also have a positive influence on the target company's external relationsships. For instance, sales volume in some of the ongoing business relationships may increase after an acquisition. Furthermore, a corporate acquisition can also lead to the reactivation of the target company's former business relationships.

In spite of the relevance of the matter, few studies are found that focus on the reactivation of business relationships (see Polonsky et al., 2010 and Leach & Liu, 2014), implying a need for further research. Therefore, in this paper our purpose is to elaborate on the reactivation process, and especially the importance of "relationship infrastructure" for reactivation. The discussion is based on two ongoing case studies of reactivation of business relationships after a corporate acquisition. The first case deals with a situation when a former employee acquires a company following bankruptcy, and how this entails that a previously terminated customer relationship is reactivated after the acquisition. In this case the reactivation is implemented within an existing "relationship infrastructure". The second case, in turn, deals with a situation when a newly established company decides to reopen a mining field. As the mine and all related business relationships were closed 20 years earlier, there is no exisiting "relationship infrastructure". Thus, the two cases differ regarding how business relationship reactivation can be implemented.

The case studies indicate that corporate acquisitions may lead to radical changes in business networks. Whereas earlier findings discuss termination effects, the study at hand focuses on reactivation effects, dealing with the impact of the existing or non-existing relationhip infrastructure for relationship reactivation.

2. Theoretical framework

2.1 Relationship infrastructure

Johanson and Mattsson (1992) note that an important issue in buying another firm "… is whether the buying firm can get control of the other firm's exchange relationships. In other words can the focal firm take over the position as well as the resources" (p. 217). Also, Anderson, Havila & Salmi (2001), Holtström (2009) and Öberg (2008) focus on this type of "network effects" (Håkansson & Snehota, 1995) of acquisitions. We know that, as business relationships are connected, the effects of an acquisition may spread into connected relations (Holtström & Öberg, 2006). An acquisition may, for example, strengthen and develop the supplier and customer relationships, or it can lead to the opposite situation: the supplier and customer relationships may deteriorate or even be terminated. Thus, we can find both positive and negative, as well as intended and unintended, effects of corporate acquisitions (Havila & Salmi, 2002).

One type of intended network effect is a reactivation of former business relationships after an acquisition. The acquisition process may function as a critical episode (Gidhagen, 2002), something that may break long term increamental processes (in e.g. relationships) into more radical changes in the network structure (Hadjikhani et al., 2013). Earlier research (see e.g. Shrivastava, 1986) has also pointed out that in the pre-merger phase all relevant stakeholders should be provided with general information about the likely impact of the merger, in order to alleviate fears about possible future changes.

In this paper we study relationships from a network perspective, i.e. each relationship is embedded in or connected to some other relationships, and as stated by Håkansson and Snehota (1995:3) "its development and functions cannot be properly understood if these connections are disregarded". Hence, in order to understand the reactivation process of relationships following an acquisition, we study what we have chosen to term the relationship infrastructure. The Merriam-Webster dictionary define an infrastructure as the underlying foundations or basic framework of e.g. a system or an organization (in our case of a relationship). It is also explained that an infrastructure can be perceived as the resources (personnel, buildings, or equipment) required for the performance of an activity. According to the definition found in Wikipedia.com (retrieved 2015-04-15) the term “infrastructure” refers to the fundamental facilities and systems serving a country, city, or area, including the services and facilities necessary for its economy to function. It typically characterises technical structures such as roads, bridges, tunnels, water supply, sewers, electrical grids, telecommunications, and so forth, and can be defined as "the physical components of interrelated systems providing commodities and services essential to enable, sustain, or enhance societal living conditions." One might also consider a “critical infrastructure”, thereby distinguishing the infrastructure elements “that, if significantly damaged or destroyed, would cause serious disruption of the dependent system or organization” (here: of the dependent relationship) (Ibid.). We assert relationship reactiviation as being embedded in a relationship infrastructure of connected resources that constitutes the basic framework of the focal relationship. The simple argumentation put forward and analysed in the paper is that an existing infrastructure is advantageous to relationship reactivation, compared to a situation where such infrastructure is missing.

Next, we present two cases studies that differ regarding the length of time of resource inactivity (i.e. the time between termination of a business relationship and the reactivation of it). In the first case, all relationships were terminated twenty years earlier. In the second case, in turn, only one relationship was terminated to later be reactivated. After the case presentations, we elaborate on relationship reactivation through corporate acquisitions and on how reactivation of business relationships is affected by relationship infrastructures.

3. Method

In order to elaborate on relationship reactivation processes, and especially on the importance of “relationship infrastructure” for reactivation, we have chosen to use a case study design. Case studies are preferable in situations where the boundaries between phenomenon and context are not clearly evident (Yin, 1984:25). In this study the whole purpose is to study a phenomenon – the reactivation of relationships – from a holistic perspective – how it is affected by the relationship infrastructure. In doing so we hope to find underlying mechanisms that shape patterning in the reactivation process (cf. Pettigrew, 1997:339). The two cases discussed herein are chosen as they are both considering acquisitions and relationship reactivation.

The first case, the Nerike Case, deals with the reactivation of the relationship between the supplier Nerike Mekan (former Örebrokugg) and the customer Sepson. The relationship between the two companies had ended in 2009 and attempts of a reactivation was started in 2011 after an acquistition of the company filed for bankruptcy. Important informants to capture and understand this reactivation process have been the CEO of both companies. In total ten interviews (mainly personal, but some telephone interviews) have been made with representatives of both the supplier and the customer. The questions asked at the interviews dealt with the reactivation process from the respondents' respective perspectives, and the interviews, structured as rather open discussions that lasted for approximately 90 minutes.

The second case, the Mining Field Case, deals with the re-opening of a Swedish iron-ore mine in 2012, 20 years after the end of prior operations. Between 2010 and 2014, two interviews were made with one of the founders of the Mining Facility (also acting as the CEO during the startup phase; each of the three subsequent CEOs were interviewed, and two interviews were made with key representatives of the local municipality in which the mining field is situated.

4.Two cases of business-relationship reactivation after a corporate acquisition

4.1 The case with existing relationship infrastructure: Nerike

In 2010, after a long period struggling financially, the company Örebrokugg was filed for bankruptcy. One year earlier, in 2009, the company went through a rigorous internal restructuring and the management decided to increase the price of its products. This change had a negative effect in the relationship with the customer Sepson. The CEO at Sepson stressed:

> "Prices were increased by roughly 30 per cent and we were not able to deal with this dramatic change. We informed the supplier about our concerns but they kept on increasing prices. This was a long process and price was just an issue that led to other concerns. Our trust for the

> supplier started to decrease substantially. It became very hard to work with them under these conditions."

Sepson decided to look for another supplier, which accepted the conditions regarding prices, products, quality and deliveries. According to Sepson´s CEO:

> "This situation was complicated for us because we had to spend a lot of time and other important resources, not only to try to solve the situation with Örebrokugg but also to find another supplier to replace them. This is not easy."

For example, Örebrokugg had made several adaptations and investments in its production plant, mechanical equipment, manufacturing processes and routines to produce specially customized products and meet the requirements of its customer Sepson. This is highlighted by the former sales manager at Nerike:

> "During this period, Örebrokugg developed several industrial products with specific features explicitly designed for Sepson. We could not sell these products to other customers because Sepson owned the rights."

After nearly fifteen years of working together and several months of discussions, the relationship between Sepson and Örebrokugg was dissolved. Although Örebrokugg tried to win-back the customer by lowering the price again, the CEO at Sepson emphasized that:

> "When we received the new offer, it was too late as we already had lost trust and confidence in the supplier. When this happens, it is very difficult to go back to that supplier so we declined the offer."

Soon after Örebrokugg's bankruptcy, a former employee acquired the bankrupt company and became the new CEO. The management team was changed and the firm was renamed "Nerike Mekan AB" (Nerike) to avoid negative associations with the bankrupted firm. All employees at the production facility were retained after the acquisition as they were considered to be valuable assets due to their special skills and capabilities in production. Even some employees in production that had been laid off before the bankruptcy were reemployed. These employees were considered to be important because they had unique knowledge and information about Nerike´s operations and customers.

In 2014, Nerike has 18 employees and a turnover of around 2, 6 million Euro. Nerike specializes in production of industrial products such as gear wheels, splines, racks, worm wheels, chain wheels and timing belt pulleys, selling to customers such as Sepson. Sepson is one of the world's leading manufacturers of hydraulic winches and systems for civilian and military users. In 2014, it employed 15 persons and had a turnover of around 7 million Euro. Under the reorganization, the new management at Nerike realized that before breaking the relation, Sepson accounted for more than ten per cent of the total turnover. Unused machinery and manufacturing equipment in the production plant that had only been used to manufacture products for this particular customer was also discovered. The CEO at Nerike highlighted:

> "These resources were regarded as wasted, as they could not be used for other purposes. We decided to take action and made several changes to revive these machines. It is very costly for a firm to have machinery that is not being in used. Personnel at the production site were also aware of this issue."

The new owner realized that existing machinery and manufacturing equipment in the production plant along with modifications in price, could contribute considerably to regain Sepson and reactivate the business relationship between the firms. Nerike made additional adaptations in manufacturing and accomplished to decrease production costs to meet Sepson´s price requirements. The production manager at Nerike pinpointed:

> "When we had made these changes, the next step was to approach Sepson and let them know that we were still reliable and that we could meet their expectations."

Past business exchanges had evidently left some traces. After the dissolution, both firms preserved manufacturing processes, routines, delivery procedures, blueprints, documents and specifically adapted products developed during their past business commitments. The CEO at Sepson explained:

> "Although our relationship with Nerike had been broken, we maintained an amount of information about this supplier because it did not make sense to get rid of it. This type of commercial information is always good to keep in the archives."

Both firms emphasized that previously developed products, along with prior experiences of business interactions and expectations of future business activities were crucial in the decision to reactivate the relation. As the purchasing manager at Sepson pointed out:

> “Nerike had delivered high quality products in the past and always on time - the company was reliable. It felt positive to go back. We had substantial prior knowledge about the supplier, their products and production capabilities.”

From the customer point of view, past business experiences and the supplier´s substantial knowledge about manufacturing customized products have been important reasons for the reactivation of the business relation. From the supplier perspective, previous adaptations in its manufacturing plant, unused equipment remaining from earlier business interactions and the importance of the customer for its total turnover had a critical role. At the same time, the relationship with Sepson allowed Nerike to purchase larger amount of raw material at a lower price, which contributed to decrease production costs for other customers. The CEO at Nerike clarified:

> “Having Sepson requires the use of more raw materials, so we negotiated a better price for larger volumes of raw material with our suppliers. By purchasing higher volumes of raw material, we have been able to decrease our production costs.”

After various discussions, the firms agreed to reactivate their business relationship. Currently, Sepson is purchasing from Nerike.

4.2 The case with limited relationship infrastructure: Mining field

Located in an area of Sweden known for its iron ore and iron works since the Middle Ages, the mining field and its iron-ore mine has been operational on a relatively large scale since the 15th century. Ownership has switched during the centuries, but the Crown/Government has always been influencing the business. The last previous owner was a large and mainly state-owned company. As a result of the low market prices paid and a weakening demand for iron ore during the late 1980s, and low or negative profit of the company, the owners decided in 1987 to close the Mining Facility. The process of closing operations, and ending/exiting extant relationships with customers, suppliers, partners, municipality officials, not to mention the employees, consequently lasted five years, until the company was left completely non-operational in 1992.

In March 2005, two entrepreneurs started a new company using the old name of the mine ("The Mining Facility"). These two entrepreneurs realized that iron ore prices were on the way up, which meant that it should be easy to finance a new operation. After studying old document archives, one of the entrepreneurs found that there was enough iron ore left to re-start the mine. The old railway line was still in place, so and hence transportation to the nearby shipping harbor would easily solved. Thus, the two entrepreneurs saw a strong business potential in resuming mining activities.

One of the entrepreneurs had ample experience starting companies from scratch, as a business angel. The other entrepreneur was a geologist with experience from mineral extraction during 45, nationally and internationally. According to him, this experience gave him good knowledge on how to deal with banks, politicians, public officers as well as competitors. During the spring of 2005, first contacts were made with public officials and politicians at the local municipality. These individuals were positive to the idea of re-starting the old mine. Also people living in and around the municipality were positive, as it would mean new employmentopportunities.

The exploitation concession was granted by the Mining Inspectorate of Sweden in 2006, after a short process,. At this point the company started also to employ people for the planning for the re-start of operations. Negotiations with local and regional authorities, as well as with Governmental agencies, were successfully managed, at the same time as relationships with potential customers and suppliers were initiated and established. Letters of intent were signed with some of the possible future customers, and in 2009 the first iron ore sample products were sent to possible customers. Finally, in 2012, the mine was fully operational and officially reopened.

During the starting process, some of the former relationships (of the previous days of business) were reactivated, such as for example with the Governmental authorities.The Government is always involved in mining activities in Sweden. Representatives of the local municipality also played an important role. For example, a local public official who had been involved in the closing process of the former company, was also involved in the reactivation of the business.

The suppliers of electricity, transport facilities, maintenance services and equipment were basically the same as they hade been 20 years ago. Furthermore, the presently potential customers were also basically the same companies as before, at the same locations and undertaking similar operations – although in some cases ownership had changed. Also present from before were actors at the shipping harbor. Many of these actors were in different ways resuming relationships with the Mining Company, even though conditions, names and – most importantly – individuals had changed. As no current relationship infrastructure was present, developing, resuming or re-developing relationships with relevant actors were all in some way influenced by whatever remains there was of relationships; be that the traditions and folklore of people in the community; customers' archival data stipulating the exact quality of what the mine could produce, or, on rare occasions, actual experience from previous mining operations at the very facility.

5. Analysis

The two cases that have been presented have several things in common: They both deal with the reactivation of relationships that took place after an acquisition. In both cases the acquired company had been out of business before it was acquired, so in neither case is it ongoing business relationships that the target had at the time of the acquisition. There are however large differences between the cases in the time dimension. In the first case, the focal 30 years old business relationship had been ended in 2009, the target company had been declared bankrupt in 2010, and the reactivation started in 2012 soon after the acquisition. Thus, the time that the target company had been out of business was short as were the time that the two companies in the focal relationships had been off doing business together.

The second case contains larger time laps: The shutting down of business was finalised in 1992, and the mine was acquired and reopened twenty years later, in 2012. The reactivation of some former relationships started around the same time, parallel to the start of new relationships. This was, hence, more a "starting from scratch" situation in network terms despite the existence of a large and functioning resource constellation (the mine with its iron ore, the railway line, mining installations, machinery etc.) at the mine. In fact it was these resources in general and the existence of iron in the mill in particular (combined with the price situation on the market for iron) that made the acquiring company interested. The case also illustrates that they were aware of the fact that the infrastructure for all relationships to potential suppliers and customers was missing at the time of the acquisition, but regarded that as a possibility to learn how to deal with banks, politicians, public officers etc.

The short time between ending and reactivation in our first case meant that a lot of the relationship infrastructure was still in place and possible to use again. It is shown in the case how previous adaptations in the supplier's manufacturing plant and its unused equipment remaining from earlier business interactions was important considerations that spoke in favour of reactivating the relationship. The fact that the relationship to Sepson allowed Nerike to purchase raw material at lower prices which contributed to decrease production costs for other customers was of course important for Nerikes interest in the reactivation as well. The possibility to reach structural economical effects are thus demonstrated in the first of our two cases, whereas both the help from a functioning infrastructure and the possibility to reach positive scal effects are much smaller in our second case.

6. Concluding remarks

The two cases presented in this paper indicate that corporate acquisitions may cause radical changes in business networks. Whereas earlier findings show termination effects, this study has focused on reactivation effects, dealing with the impact of the existing or non-existing relationship infrastructure on relationship reactivation. Our two cases show that the reactivation of a relationhip is depending on if there is or isn't any relationship infrastructure to fall back on. In our first case the many historical investments that have been made in the relationships make it relatively easy and economically reasonable to reactivate the relationship. The second case, however, describes a business situation without a functioning relationship infrastructure. Much time and effort need here to be invested in this infrastructure in order to reach beneficial business relationships. Our simple conclusion is, hence, that the aspect of relationship infrastructure is essential to the reactivation of business relationships after acquisitions.

References

Anderson, H., Havila, V. & Salmi, A. (2001). Can You Buy a Business Relationship? On The Importance of Customer and Supplier Relationships in Acquisitions. *Industrial Marketing Management,* 30, 575-586.

Gidhagen, M. (2002). *Critical Business Episodes. The Criticality of Damage Adjustment Processes in Insurance Relationships*. Uppsala: Department of Buiness Studies.

Hadjikhani, A., Hadjikhani, A.I. & Thilenius, P. (2013). The internationalization process model: A proposed view of firms´regular incremental and irregular non-incremental behavior, *International Business Review*, 23(1), 155-168.

Havila, V., & Salmi, A. (2002). Network perspective on international mergers and acquisitions: What more do we see?, In; *Critical Perspectives on Internationalisation*, 2002, 457-472.

Holtström, J. (2012). Supplier relationships at stake in mergers and acquisitions, in Anderson, H., Havila V. and Nilsson, F. (eds.), *Mergers and Acquisitions – The Critical Role of Stakeholders*, New York: Routledge, 168-184.

Håkansson, H. & Snehota, I. (1995). (eds.) *Developing Relationships in Business Networks*, London: Routledge.

Johanson, J. & Mattsson, L.-G. (1992). Network positions and strategic action – an analytical framework, in Axelsson, B. & Easton, G. (eds.), *Industrial Networks*, London : Routledge, 205-217.

Leach M. P. & Liu, A. H. (2014). It aint' over 'till it's over: Evaluating reacquisition opportunities in business-to-business markets. *Industrial Marketing Management*, 43, 573-581.

Pettigrew, A. M. (1997). What is a processual analysis?, *Scandinavian Journal of Mangement*, 13 (4), 697-713.

Polonsky, M., Gupta, S., Beldona, S., & Hyman, M. R. (2010). Inactivity and the dynamics of relationship development: a proposed model. *Journal of Strategic Marketing,* 3, 257-273.

Shivastava, P. (1986). Postmerger integration. *The Journal of Business Strategy,* 1, 65-76.

Yin, R. K. (1984) *Case Study Research: design and methods*, Bevely Hills, California: Sage.

Öberg, C. & Holtström, J. (2006). Are mergers and acquisitions contagious? *Journal of Business Review*, 59(12), 1267-1275.

Öberg, C. (2012). Why do customers dissolve their business relationships with the acquired party following an acquisition?, in Anderson, H., Havila V. and Nilsson, F. (eds.), *Mergers and Acquisitions – The Critical Role of Stakeholders,* New York: Routledge, 183-202.