

Fall 2014

The Effects Of Acquisition On Restaurant Firms' Performance: Different-Sector Versus Same-sector Acquisitions

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**PURDUE UNIVERSITY
GRADUATE SCHOOL
Thesis/Dissertation Acceptance**

This is to certify that the thesis/dissertation prepared

By YONGJIN LEE

Entitled

THE EFFECTS OF ACQUISITIONS ON RESTAURANT FIRMS' PERFORMANCE:
DEFFERENT-SECTOR VERSUS SAME-SECTOR ACQUISITIONS

For the degree of Master of Science

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8/28/2104

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Date

THE EFFECTS OF ACQUISITION ON RESTAURANT FIRMS' PERFORMANCE:
DIFFERENT-SECTOR VERSUS SAME-SECTOR ACQUISITIONS

A Thesis

Submitted to the Faculty

of

Purdue University

by

Yongjin Lee

In Partial Fulfillment of the

Requirements for the Degree

of

Master of Science

December 2014

Purdue University

West Lafayette, Indiana

ACKNOWLEDGEMENTS

Major research like this is never the work of anyone alone. The contributions of many different people, in their different ways, have made this work possible. I would like to extend my appreciation especially to the following people. I thank God for the wisdom and perseverance that he has been bestowed upon me during this thesis and, indeed, throughout my life: “I can do everything through him who give me strength” (Philippians 4:13).

I am especially grateful for the guidance, support, advice, and patience of my major professor at Purdue, Dr. Chun-Hung (Hugo) Tang. Without his guidance, I would not have been able to put the topic together.

My thanks also to my committee members who were also my professors, Dr. Carl Behnke and Shawn Jang, for their support and encouragement. Their insightful comments and constructive criticisms at different stages of my thesis were thought provoking.

I am also grateful to my friend, Dr. Jeongyeol Park. His support and care helped me overcome setbacks and stay focused on my graduate studies.

Last but not least, I would like to thank my wife who had to endure the unforeseen limitations of a student husband for her unconditional support, both financially and emotionally, throughout my degree.

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ABSTRACT

Lee, Yongjin. M.S., Purdue University, December 2014. The Effects of Acquisition on Restaurant Firms' Performance: Different-Sector versus Same-Sector Acquisitions. Major Professor: Chun-Hung (Hugo) Tang.

This study examines the postacquisition accounting performance of acquiring firms in the restaurant industry between 1992 and 2012. Specifically, this study investigates the effects of different-sector and same-sector restaurants acquisitions between full-service and limited-service restaurants on restaurant firms' performance. Additionally, the Wilcoxon signed-rank test and regression model are used to examine return on assets (ROA) and return on equity (ROE) for the accounting performance of the acquiring restaurants.

The ROA and ROE reveal that the profitability is significantly negative up to 5 years after firms are acquired. However, negative effects are strongest within the first year after acquisition and decrease until 4 years after compared with previous years. After 4 years, the negative effects turn to positive compared to the previous year for ROA and ROE changes.

Further, the study reveals that the difference between different-sector and same-sector acquisitions indicates no significant relationship between ROA and ROE changes during all 5-year periods. Overall, this study shows that the effects of acquisitions between

different sectors and the same sector are negative and there is no significant difference between them.

CHAPTER 1. INTRODUCTION

1.1 Introduction

During the early 1950s, the restaurant industry emerged as one of the fastest-developing industries in the United States. Total sales growth increased from US\$42.8 billion to an estimated US\$586.7 billion between 1970 and 2010, which represents an annual average sale growth rate of about 32% (National Restaurant Association, 2010). Total sales growth was predicted to be US\$683.4 billion by 2014 (National Restaurant Association, 2013).

Due to severe market saturation and low entry barriers, restaurant firms constantly need to pursue fast-growing strategies to survive and maintain competitiveness. Restaurant firms' compulsion to grow quickly may be reflected in the merger and acquisition (M&A) phenomenon during the last decade. The restaurant industry experienced considerable M&A activity in the 1990s (Chatfield, Dalbor, & Ramdeen, 2011), and the Chapman Group (2008) reported that 78 M&A transactions occurred among restaurant firms in 2003. That number increased to 112 in 2007. However, the M&A restaurant waves began earlier in 1985 (Harford, 2005).

Conventional wisdom often considers M&As an effective growth strategy (Hsu & Jang, 2007) since efficient execution replaces the acquired firm's inefficient resources with the acquiring firm's superior resources (Trautwein, 1990). Montgomery and Singh

(1984) explained that M&As can increase market power and increased market power leads to more excess returns when a company has the ability to influence the price, quantity, and quality of products in the marketplace. Kiymaz (2004) also suggested that M&As contribute to growth, market expansion, and lower financing costs. However, acquisitions are not necessarily an effective tool for producing consistent growth in restaurant firms. Enormous barriers must be controlled to realize faster growth. Acquisitions involve a time-consuming process, and the real chemical integration required to achieve synergy is hard to accomplish (David & Singh, 1994). For example, the degree of the relatedness of the two firms, both operationally and culturally, varies among the acquiring and target firms, which affects the success of the M&A (Canina, Kim, & Ma, 2010). The target firm's and the acquiring firm's financial conditions, size, and location and the type of deal are also closely related to the success of the M&A (Kim & Olsen, 1999). Further, the duration of the M&A effect is still controversial, even after the transaction has been completed (Park & Jang, 2011; Yang, Qu, & Gu, 2009). Thus, most researchers have identified negative M&A effects for acquiring firms in the hospitality industry in contrast to conventional M&A benefits (Hsu & Jang, 2007; Canina et al., 2010; Chatfield & Delbor, 2011).

However, since previous studies examined the effect of M&As from only the financial perspective, the results might be too limited to fully understand the various effects of M&As on firm performance in the restaurant industry. Additionally, in terms of the effect of M&As on firm performance, several studies have revealed that M&As had a positive influence on the acquiring and target firms in the lodging industry (Canina, 2001; Kim & Canina, 2013; Yang et al., 2009). Scholars did not fully explain U.S. restaurant

firms' use of M&As as a growth strategy since from 1992 to 2012 many restaurants extended their businesses through M&As. Therefore, more specific research models must be developed to understand restaurant firms' post-M&A benefits along with the increased M&A transactions.

In the restaurant industry, M&As occur between restaurants. In this industry, restaurants are divided into two categories: full service and limited service. There are distinctive differences in financial characteristics between full-service and limited-service restaurants in terms of their financial and operational resources (Gu, 1993; Petraf, 1993; Tse & Olsen, 1988; Walker & Johnson, 2002). The varying financial and operational resources influence restaurants' accounting performance differently (McCool & Gu 1993; Youn & Gu, 2010). For example, the degree of standardization of the restaurant operation process, the level of employee skill, advertisement expense, and food costs are quite different between full-service and limited-service restaurants. Therefore, investigating the effects of acquisition is important to understand which types of acquisitions between full-service and limited-service restaurants improve accounting performance.

The primary purpose of this study is to examine the effects of acquisition on firms' accounting performance among different restaurant sectors. The study categorizes acquisitions into two distinctive types, which are different-sector (full-service or limited-service restaurants acquire limited-service or full-service restaurants) and same-sector acquisitions (full-service or limited-service restaurants acquire full-service or limited-service restaurants), since each restaurant sector has different operating and financing characteristics.

This study investigates the effects of acquisitions on the firm performance of the restaurant industry by comparing the two sectors. Consequently, this study tries to identify the different postacquiring accounting performance between different-sector and same-sector acquisitions and suggest which types of acquisition are better for the acquiring firms' profitability (return on assets [ROA] and return on equity [ROE]).

1.2 Study Objectives and Research Questions

The purpose of this study was to investigate the effects of acquisitions on restaurant firms and to compare the performances of the restaurant sectors. Generally, restaurants are classified as full-service and limited-service restaurants. Acquisitions between full-service restaurants and limited-service restaurants are classified as different-sector and same-sector sector acquisitions. When a full-service restaurant acquires a limited-service restaurant, the acquisition is identified as a different-sector acquisition because the acquisition occurs in a different sector. When a full-service restaurant acquires a full-service restaurant, the acquisition is identified as a same-sector acquisition because the acquisition occurs in the same sector. In addition, the acquisition is related to resource-based views of the firm because each sector has different resources.

An analytical framework that will improve industry participants' understanding of acquisitions among different segments of restaurants and the influence of strategic decisions on the firm's performance connection is proposed. The following research questions focused this study: (a) Does the postacquisition period of acquiring other restaurants significantly influence accounting performance? (b) Which type of

acquisition, different sector or same sector, more significantly influences firm performance? The study questions are shown in Table 1.1.

Table 1.1. Types of Restaurant Acquisitions

		Acquisitions	
		Different-sector acquisitions	Same-sector acquisitions
Restaurant Type	Full-service	Full-service restaurants acquire limited-service restaurants	Full-service restaurants acquire full-service restaurants
	Limited-service	Limited-service restaurants acquires full-service restaurants	Limited-service restaurants acquire limited-service restaurants

1.3 Justification

Before firm accounting performance is examined through acquisitions, the restaurant industry must be evaluated in terms of the differences between restaurant sectors as a whole. Several studies have suggested that restaurants differ across sectors in terms of organizational environment and financial performance. In limited-service restaurants, standardization of food such as taste, packing, and operating system is higher than in full-service restaurants (National Restaurant Association, 2010). Walker and Johnson (2002) reported that full-service restaurants are more labor intensive than limited-service restaurants. The researchers also suggested that the labor costs of full-service restaurants are higher than those of limited-service restaurants. Gu and McCool (1993) showed that inventory turnover and debt financing differ between full-service and limited-service restaurants. Full-service restaurants have lower advertisement expenses than limited-service restaurants. Additionally, the Franchise Finance Corporation of America (FFCA; 2001) showed that full-service restaurants spent about half the

percentage of their sales on advertising compared with limited-service restaurants.

Limited-service restaurants are more robust in economic or market downturns than full-service restaurants (FFCA, 2001). Thus, the sectors' resources differ.

Acquisition is one diversification strategy and can be followed by theoretical resource-based views. In other words, the effects of acquisition on the restaurant sectors might differently influence a firm's operating performance depending on whether the acquisition is made in different sectors or the same sector because different or similar resources are combined in an acquisition. Although many scholars have asserted that the advantages and disadvantages depend on the diversification strategy and the acquisition itself, recently, only a few studies on restaurant sectors have shown their different financing and operating characteristics. Several scholars have suggested that acquisitions affect firm performance in the restaurant industry. However, the effects of acquisitions between restaurant sectors are likely to differently influence firm performance based on a resource-based view.

The purposes of this study are to investigate the effects of acquisition on firm performance over the 1992 through 2012 period and to analyze the accounting performance of the two restaurant sectors. To further identify the effects of acquisitions on firm performance, the effects between restaurant sectors must be compared. Because an acquisition is directly related to the act of a combining different or same resources to form a single firm, an investigation of differences related to the type of acquisition could be important in terms of expanding practical knowledge and contributing to acquisitions between restaurant sectors.

The study findings may help investors and managers better understand the return features of various types of restaurants and assess investment opportunities in different sectors of the restaurant industry. From these performance comparisons, restaurant executives may also find useful suggestions for implementing strategies that could help improve the firm performance of the acquisitions, and thus maximize shareholders' wealth and firm profitability.

CHAPTER 2. LITERATURE REVIEW

2.1 Overview of M&As

Finance scholars have investigated various M&A waves with increasing scale, growth, and geographic diversification. Becketti (1986) reported that the Great Merger wave rapidly increased for monopolies in 1890s. The main purpose of the M&A wave was to stabilize prices by removing competitors rather than gaining economies of scale (Lamoreaux, 1988). The second wave occurred in the 1920s so oligopolies could hold the most market power in their own industries. Although the M&A trend emerged in horizontal consolidations in the same market (Becketti, 1986), the trend was economies of scale (Martynova & Renneboog, 2008).

In the 1960s, the third wave was initiated by antitrust laws and firms' movements toward diversification (Shleifer & Vishny, 1991). The antitrust laws decreased M&A activity in the same industry and increased conglomerate M&A activity in different industries (Shleifer & Vishny, 1991). Firms in the 1960s generally used merger and acquisition strategies to enter new markets, which is unrelated diversification (Sudarsanam & Mahate, 2003). Unrelated diversification was expected to decrease the risks of volatile cash inflow as a means of developing firm value (Copeland, Weston, & Shastri, 2004; Montgomery, 1994). Acquirers created managerial synergy by obtaining management know-how from target firms (Matsusaka, 1993).

However, the low performance of the conglomerates' divisions resulted in ineffective management (Shelifer & Vishny, 1991), which triggered a fourth wave of M&As in the 1980s. Firms then focused on their main businesses, which is called related diversification (Andrade, Mitchell, & Stafford, 2001; Bhagat, Shleifer, & Vishny, 1990). In addition, deregulatory reforms allowed firms to make horizontal M&As (Martynova & Renneboog, 2008).

Last, M&A activity was more sophisticated and more geographically dispersed between 1993 and 2001 (Martynova & Renneboog, 2008). M&As opened up the global market in terms of product, service, and capital, which drove cross-border M&As (Andrade et al., 2001).

2.1.1 Motivations for M&A Activity

M&A scholars have proposed numerous motivations for why firms perform M&As. Generally, scholars categorize firms' motivations into four areas: market context, managerial power, environmental factors, and firm characteristics.

First, finance scholars have investigated the impact of market power due to increasing firm-level pricing and power because firms gain a small part of their sales in the competitive market segment. M&As helped increase market power for firms. In addition, economists suggested that M&As were motivated by the desire to increase efficiency. Firms made related diversifications or unrelated diversifications to improve their efficient productivity. Agency researchers reported M&As help shareholders minimize losses from poor management.

Second, finance and management researchers have also suggested that industries with higher chief executive officer (CEO) compensation generally show increased acquisition activity (Agrawal & Walkling, 1994). M&A deals are highly related to CEO compensation (Bliss & Rosen, 2001; Denis, Denis, & Sarin, 1997; Datta, Iskandar-Datta, & Raman, 2001; Rose & Shepard, 1994). Additionally, firms increase CEOs' power and wealth, which can establish managers and decrease their employment risk (Gomez-Mjia & Wiseman, 1997; Haleblan & Finkelstein, 1993; Hambrick & Finkelstein, 1987). Managerial power was closely tied to shareholder returns to align managers' and shareholders' interest.

Third, strategic management researchers have investigated whether the fit between environmental factors and a firm's strategy stimulates acquisitions. Environmental uncertainty encourages firms to acquire other firms to decrease uncertainty. Highly diversified firms tended to create more M&As (Bergh & Lawless, 1998). In addition, finance management scholars have suggested regulation influenced the likelihood of acquisitions (Beneish, Jansen, Lewis, & Stuart, 2008).

Last, the management literature has supported the influence of firm characteristics on M&As. Baum, Li, and Usher (2000) reported that firms acquire other corporations that were geographically and organizationally similar. Further, firms that have more acquisition experience tend to have an increased likelihood of acquiring firms (Vanhaverbeke, Duysters, & Noorderhaven, 2002). In the finance area, many scholars have widely investigated the impact of M&As on performance relationships such as deal characteristics, managerial effects, financing and accounting performance, and environmental elements.

2.1.2 Review of M&A Studies in the Hospitality Industry

Although M&As has been examined with various strategies, few researchers have addressed M&A trends in the hospitality industry. Most scholars have shown that the returns to the merger participants fluctuated over time. Jensen and Ruback (1983) suggested that corporate takeovers generated positive gains and found that the target firms gained positive returns. Andrew (1988) empirically measured most of the impact of acquisitions on a hospitality firm's value. He found that acquirers lost value during the 20 days before the acquisition was announced. In contrast, target firms gained value during the same period; however, the size of the additional wealth gained was skewed upward. Kwansa (1994) estimated the size of the additional wealth gained by the equity holders of lodging firms acquired in the 1980s. He reported that the bulk of the additional wealth was created 2 days before and after an acquisition was announced. Enz, Canina, and Walsh (2001) investigated abnormal returns for lodging firms' acquirers from 2 days before through the day after a merger was announced (-2, +1) between 1982 and 1999. The researchers found that lodging industry acquirers received positive abnormal returns on the day the merger was announced, but not before or after the announcement. Hsu and Jang (2007) asserted that most postmerger financial performances of acquiring firms in the lodging industry showed no significant relationship between the merger announcement and the change in short-term equity value, but M&As showed a significantly negative ROA and ROE after the merger for 5 years. Chatfield et al. (2011) suggested that acquiring firms have positive cumulative abnormal returns (CARs) except 1 day before the announcement and the announcement day, but target firms have positive CARs for the same period. Sheel and Nagpal (2000) reported the effect of M&As

between the short term and the long term was not significant or negative from 1980 to 2000. However, Yang et al. (2009) asserted that acquiring hospitality firms had significantly higher abnormal returns 12 months after mergers. Park and Jang (2011) investigated whether acquiring restaurant firms experienced higher growth in sales volumes than nonacquiring restaurant firms over a year; however, the effect of the M&A was not consistent after 1 year.

In addition, the types of payment for M&As have rarely been studied in the hospitality industry because the payment method can significantly influence the returns for M&A participants. Acquirers have a choice among cash, stock, or a combination of both. Oak, Andrew, and Bryant (2008) suggested that debt ratio, capital expenditure ratio, and firm size are important for deciding the appropriate finance method for an M&A. They found that cash deals were preferred for M&As in the hospitality industry. Recently, Chatfield, Chatfield, and Dalbor (2012) found that cash financing was significantly positive for earning abnormal returns in the lodging, restaurant, and gaming industries. However, when acquiring firms used mixed cash and stocks, the effect of the abnormal returns was insignificant.

2.2 Costs of Acquisitions

Acquisitions separate management from ownership in modern multiowner corporations. Firms make acquisitions even when the managerial cost of the acquisition is higher than the marginal growth in the value of the firm (Barle & Means, 1932; Baumol, 1959; Mueller, 1969; Williamson, 1975). Some researchers suggested that even though better outcomes are related to choosing a better target, negotiating a better financial deal,

and successfully sharing strategic fit and organizational fit may depend on the characteristics of the process for making acquisition decisions. Acquisition decisions are distinguished from other strategic decisions because of the risk characteristics related to some degree of uncertainty (Haspeslagh & Jemison, 1991), and the uncertainty is associated with acquisition outcomes. The high rate of failed acquisitions demonstrates the significant potential for loss (Ravenscraft & Scherer, 1987). Additionally, acquisitions have high levels of risk for decision makers because of the visibility and tendency of acquisitions to induce intense personal commitment (Haunschild, Davis-Blake, & Fichman, 1994). Morck, Shleifer, and Vishny (1990) suggested that the returns to bidding shareholders are lower when their firm diversifies, when it buys a quickly growing target, and when its managers performed poorly before the acquisition.

Generally, scholars have become concerned with developing a better understanding of the cost of specific acquisitions. In studies, the cost of acquisitions is commonly explained in terms of three categories: deal characteristics, firm characteristics, and negative returns. King, Dalton, Daily, and Covin (2004) asserted that managers finance acquisitions with cash when the managers recognize their firms are undervalued and with stock when managers recognize their firms are overvalued. Several scholars have asserted that cash-financed deals are more beneficial to bidding firms' shareholders (Carow, Heron, & Saxton, 2004; Huang & Walkling, 1987; Loughran & Vijh, 1997; Travlos, 1987). However, Heron and Lie (2002) suggested there were no significant differences in operating performance between cash and stock deals but showed lower postacquisition market returns for stock acquisitions than for cash acquisitions. Interestingly, Faccio, McConnell, and Stolin (2006) asserted that acquirer

abnormal announcement returns are higher for private firms than for public target firms. Although the types of deals in the restaurant industry have rarely been studied, some financial scholars suggested that managers of low book-to-market firms might make poorer acquisition decisions than managers of other firms. These suggestions imply that acquiring firms in the restaurant industry should consider that prior performance influences acquisition returns.

Researchers investigating the cost of acquisitions have emphasized that the influence of different cultures and political characteristics (Pablo, 1994). An emergent and growing field of inquiry is the cultural dynamics of M&As and the implications of cultural differences for the postmerger integration process (Cartwright & Schoenberg, 2006). Some scholars have sought to explain underperformance in terms of the effect that variables such as cultural distance (Morosini, Shane, & Singh, 1998), cultural fit (Weber, Shenkar, & Raveh, 1996), different management style (Datta, 1991; Larsson & Finkelstein, 1999), cultural change (Kavanagh & Ashkanasy, 2006), and cultural convergence (Birkinshaw, Bresman, & Hakanson, 2000) have on the integration process of firms engaging in M&A activity. These scholars suggested that strategic culture integration is very important between acquirers and targets to enhance synergy-influenced long-term postacquisition accounting returns.

Many scholars have also asserted that historical operating performance has a role in acquisition events. For instance, Heron and Lie (2002) suggested that postacquisition performance increased when bidders with higher market-to-book ratios acquired targets with low market-to-book ratios. Lang, Stulz, and Walkling (1989) suggested that high Tobin's Q bidders attained more than low Tobin's Q bidders and low Tobin's Q targets

benefited more from takeovers than high Tobin's Q targets. The researchers also found that bidder announcement returns were negatively associated with cash flow for low Tobin's Q bidders rather than related to cash flow for high Tobin's Q bidders. Interestingly, this finding implies that acquisition performance increases when a high-performing firm pairs with low-performing targets. Chatterjee (1992) suggested low-performing targets provide upside restructuring value, which offers the greatest opportunity for value creation in takeovers. Researchers have also asserted that firm size influences the performance of acquisitions. Healy, Palepu, and Ruback (1992) found that large mergers resulted in positive postacquisition accounting performance and increased customer satisfaction, employee productivity, and asset growth (Cornett & Tehranian, 1992).

In contrast, Moeller, Schlingemann, and Stulz (2004) found that small acquisitions by small bidders showed positive announcement gains, whereas large acquisitions by large bidders showed negative announcement losses. These studies indicated that large firms contributed larger acquisition premiums than smaller firms and suggested that large firms' acquisition decisions played a more important role than small firms' decisions. Thus, the role of firm size in the restaurant industry is an important cost factor in acquisition performance.

Some scholars have observed that acquirers earned negative returns while other scholars have asserted bidders gained positive returns for M&As. Jensen and Ruback (1983) reported an average abnormal return of -5.5% during the 12 months after takeovers. Franks, Harris, and Mayer (1988) used a comprehensive sample of U.S. and U.K. acquirers from 1955 to 1985. The researchers found that after merging firms

reported negative abnormal returns. Franks, Harris, and Titman (1991) used an equally weighted index. The results generated with multiple factor benchmarks and the eight-portfolio benchmark in particular showed no significant abnormal returns. These findings confirmed findings from earlier studies (Asquith, Bruner, & Mullins, 1987; Dodd, 1980; Langetieg, 1978; Morck et al., 1990). However, scholars have asserted that the acquiring firms' shareholders gained normal returns over the 5-year period following takeovers.

Additionally, Magenheim and Mueller (1988) and Agrawal, Jaffe, and Mandelker (1992) found that shareholders lost on average. The authors concluded managers sought to maximize firm size rather than shareholder wealth. Bradley et al. (1988) found that excess returns to acquirers after a takeover was announced decreased from about 4% in the 1960s to 1.3% in the 1970s and then to -3% in the 1980s. However, the scholars also suggested positive combined earnings for acquirers with public targets in takeovers for each period. Further, Jarrell and Poulsen (1987) and Bradley, Desai, and Kim (1988) suggested that multiple acquirers for a target were associated with significantly higher abnormal returns.

Overall, although many scholars have explored whether acquisitions contributed to firms' positive performance, product market, or capability domains, some scholars also found that due to the costs or risks of acquisitions that firms need to consider the framework of the firm's strategic direction, the similarity of their organizational cultures, top management styles, and decision-making practices.

2.3 Gains from Acquisitions

Acquisitions and mergers are still popular strategies. Since 1960, the Federal Trade Commission (FTC) has recorded more than 20,000 acquisitions and mergers. Acquisitions are generally good news for the stockholders of the acquiring firms. Benefits include economies of scale, attribution of monopoly or economic power, diversification, and increase in the stocks' market ability (Butters, Lintner, & Cary, 1951; Edwards, 1955; Levy & Sarnat, 1970; Lewellen, 1971; Lintner, 1971).

Global investment in mergers and acquisitions (hereafter referred to simply as acquisitions) has reached unprecedented levels in recent years (Barkema & Schijven, 2008). Acquisition activity in terms of monetary and strategic issues has increasingly become a focus of study in several academic fields. Although this interest has generated considerable knowledge related to acquisitions, the range of findings from these comprehensive areas lacks theoretical integration, which constrains scholars' ability to synthesize the remarkable contributions by each discipline. Acquisitions are a crucial activity for redirecting and renewing corporate strategy. Many researchers and practitioners have studied the executive as a rational decision maker, and investigated an efficient marketplace for a strategically advantageous acquisition.

Given that, why do firms undertake acquisitions? Although many scholars have argued there are many reasons for acquisitions, three criteria, including market power, efficiency, and economies of scale, are examined here. First, market power is an attempt to appropriate more value from consumers. Although an early study did not find evidence of market power as an acquisition antecedent (Eckbo, 1983; Stillman, 1983), some researchers have found the effect through increasing stock prices and highly diversified

firms. In general, mergers due to strategic management may improve the performance of the acquiring firm in an industrial organization. Mergers can be identified from the contingency framework for diversification strategies as described in strategic management studies (Christensen, Berg, & Salter, 1976; Rumelt, 1974) because mergers show diversification activity. An acquiring firm merges to achieve competitive strengths and improve the growth rate of the firm's markets with the acquired firm. In addition, the more similar the environments of the two firms, the greater the performance profit for the acquired firm. The FTC classifies mergers as horizontal, vertical, product, or market concentric, or conglomerate, which indicates the amount of strategic fit achieved in a merger.

Second, acquisitions are motivated by the desire to increase efficiency. Efficiency that reduces the cost of creating value results from improvements in long-term plant productivity (McGuckin & Nguyen, 1995) and public accounting service delivery (Banker, Chang, & Cunningham, 2003). Management scholars have shown managerial interest in an acquisition. Acquisitions increase managerial value since managers attempt to maximize their own interest.

Third, Capron, Dussauge, and Mitchell (1998) suggested that managers view acquisitions as a means of promoting redeployment of assets and competence transfers to generate economies of scope. King, Slotegraaf, and Kesner (2008) showed that acquirer abnormal returns were associated with the degree of the acquirer and target firm resource complementarity. Redeploying resources enables acquirers to add to existing strengths and extend resources into new parts, and it contributes to economies of scale. Additionally, managers may use acquisitions as a means of innovation with their

resources. The market position and resources of firms involved in acquisitions affect future product market performance (Lubatkin, Schulze, Mainkar, & Cotterill, 2001). The empirical results show that synergy is the primary motive in takeovers with a positive relationship between the target and total gains. Thus, M&As do pay.

2.4 Diversification

Researchers have investigated the effect of unrelated diversification and related diversification. Firm diversification has been a widely accepted strategy in U.S. industry. In the current study, acquisitions are associated with unrelated and related diversification because restaurant firms diversify resources to enter sectors different from the firms' own within the restaurant industry.

Ansoff (1957) first used the term "diversification" to demonstrate corporate growth strategies involving entering new markets with a new product. Berry (1971) indicated diversification was an increase in the number of industries in which a business participates. Dundas and Richardson (1980) argued that when firms diversify, they differentiate markets and pursue more than one target market. This is one of the most frequently used definitions of diversification.

According to Amit and Livnat (1988), diversifying business combinations helps increase the size of the business, accomplishes an economy of scale in manufacturing, marketing, and research and development (R&D), and thus produces synergic effects for an overall operation. Chatterjee and Wernerfelt (1991) contended that through diversification companies seek to utilize excessive resources of current performances for extra earnings. Montgomery (1994) illustrates three main theoretical perspectives that can

be used to explain why a firm might choose to diversify: agency theory, the resource-based view, and market power.

From the agency cost theory, managers may seek to diversify because it is expected to (1) expand their compensation (Jensen & Murphy, 1990), power, and prestige (Jensen, 1986); (2) make their positions with the firm more secure or less volatile by making investments that require their particular skills via manager-specific investments (Shleifer & Vishny, 1991); or (3) reduce the risk of their personal investment portfolio by reducing firm risk since the managers cannot reduce their own risk by diversifying their portfolios (Amihud & Lev, 1981).

In the resource-based view, rent-seeking firms diversify in response to excess capacity in resources such as productive factors. According to Penrose (1959), a diversified firm is an efficient form for organizing economic activities. For instance, the firm may use the same marketing and distribution channel to market a variety of goods or services. Montgomery and Wernerfelt (1988) noted that a firm's resources differ in terms of specificity. For example, more specific resources, such as productive skills in biotechnology, may be efficiently applied in only a small number of industries but may yield higher marginal returns because of their specificity unlike less specific factors such as standard-issue machines. In other words, for a firm with less specific resources, profits may be maximized at a relatively high level of diversification even though a firm with more specific resources could obtain higher profits with less diversification.

From the market power perspectives, this perspective argues that the large diversified firm in terms of conglomerate power is market power. A firm may be able to

exploit, extend, or defend its power by tactics other than those that are traditionally associated with the view of monopoly.

Villalonga (2000) offered three anticompetitive motives for diversification. First, one industry uses the profits generated with predatory pricing policy in another industry. The second stimulus involves colluding with other firms that compete with the firm in the market. Finally, firms may use corporate diversification to participate in reciprocal buying with other large firms to drive out smaller competitors. Additionally, Rumelt (1974) claimed that diversification could be understood as an aggregation of two or more income streams.

However, Datta, Rajagopalan, and Rasheed (1991) argued that previous researchers overlooked industry structure (e.g., industry competition, concentration, growth rate, and profitability). This means that the performance of diversification strategies depends on the performance of the target industry.

2.5 Unrelated Diversification

Several scholars have suggested that unrelated diversified firms performed better than related firms (Luffuman & Reed, 1984; Michel & Shaked, 1984). Because the earnings streams from related diversification are significantly correlated based on business segment diversification (e.g., earlier-than-expected technological obsolescence of a similar production technology), it is unlikely that risk will be largely reduced. In addition, unrelated diversification could be more profitable than related diversification because unrelated diversified firms are in a better position to reduce the cost of capital and optimally invest (Hill & Snell, 1988).

Going further, unrelated strategies might present some unique advantages of their own derived primarily from financial synergies. For example, portfolio theory suggests that industry-specific risk can be reduced only through extraindustry diversification (Kim, Hwang, & Burgers, 1989). Therefore, unrelated diversification can do more to reduce risk since this strategy involves business units in multiple industries (Amit & Livnat, 1988). Though some scholars (Lubatkin & Rogers, 1989) would take issue with this position by arguing that related firms enjoy reduced risk owing to their superior competitive advantage, on balance, most still believe risk reduction is a greater advantage for unrelated diversifiers (Barney, 1997).

Furthermore, the lower risk that results from portfolio effects and reduced probabilities of bankruptcy can also lead to increased debt capacity (Seth, 1990). These firms may also enjoy the windfall of reduced taxes, even in the absence of operational synergies because interest expenses are tax deductible. As a result, lower operating risk is associated with more stable cash flows and increased levels of leverage (Amit & Livnat, 1988).

Recent conceptual developments in strategy have focused on diversification using a resource-based view of the firm (Barney, 1991; Foss, 1998; Wernerfelt, 1984). This method views the firms as a bundle of heterogeneous and imperfectly mobile resources (Wade & Gravill, 2003). Mobility is defined as resources that “can be bought and sold in factor markets” (Barney, 1991). Under this condition, the resources enable the firm to obtain sustained competitive advantage. The resource-based view of diversified corporations ultimately lies in sharing strategic assets and capabilities among entities (Mahoney & Pandian, 1992; Teece, 1982) rather than simply reducing transactions costs.

In terms of the resource-based view, resources are more easily shared in related diversification than in unrelated diversification (Capron & Hulland, 1999). Efficiently shared resources mean firms are expected to perform better than the sum of the separate resources in the business (Coase, 1937; Robins, 1992; Teece, 1984).

The type of diversification that might result from a resource depends on its specificity in a particular industry (Gorecki, 1975; Grabowski & McGuckin, 1985; Montgomery & Wernerfelt, 1988). If a resource can be used to produce only one product, then the resource is not suitable for diversification. However, most resources can be used for more than one end product (Chatterjee & Wernerfelt, 1991). According to the substantial tradition in the literature (Macdonald, 1984; Montgomery & Hariharan, 1990; Teece, 1982), to make related or unrelated diversification work, three classes of resources are required: (a) physical resources, (b) intangible assets, and (c) financial resources.

A firm's physical resources, such as a plant and equipment, are characterized as fixed capacity. They are generally useful in similar industries. If excess physical capacity motivates diversification, industries closely related to those in which the capacity is being used would be included (Chatterjee & Wernerfelt, 1991). Barton (1998) and Bettis (1981) suggested that capital expenditures were associated with related diversification.

Intangible assets include brands and human skills. A brand name can be applied to several products with little or no adverse effects on existing applications. Similarly, a strong marketing team could successfully market in different markets without risk to the brand of the original business. A motivation for intangible assets is to present a developed approach that captures the skill base of relatedness (Farjoun, 1994), in particular, human skills shared by researchers interested in the resource-based view

(Barney, 1991; Mahoney & Pandian, 1992; Penrose, 1959; Teece, 1982; Wernerfelt, 1984), and by practitioners who view these resources as essential to firm success (Hall, 1992).

In general, financial resources are the most flexible of all resources because the resources can be used to buy all other types of productive resources. Financial resources can be classified as internal funds and external funds (Chatterjee & Wernerfelt, 1991). Internal funds consists of liquidity at hand and unused debt capacity to borrow at normal rates. External funds consist of new equity and possibly high-risk debts. Several researchers found that lower levels of internal funds lead to lower levels of unrelated diversification and vice versa (Chatterjee & Wernerfelt, 1991). Since unrelated diversification tends to be considered risky by the capital market (Barton, 1988; Lubatkin & O'Neill, 1987; Montgomery & Singh, 1984), external funds would not generally be available for unrelated diversification.

The general belief is that physical resources and intangible resources are associated with related diversification, while financial resources are associated with unrelated diversification (Coase, 1937; Teece, 1982). Empirical evidence finds organizations diversify more broadly than predicted by Penrose (1959) and other modern resource-based approaches (Teece et al., 1997). Various researchers recognized an organization's heterogeneous resources are key to explaining the behavior and performance of large diversified firms (Montgomery, 1994; Montgomery & Hariharan, 1991; Teece, 1982), and thus, a conceptual model that integrates Penrose's (1959) resource-based approach with an incomplete market approach (Denrell, Fang, & Winter, 2003) was proposed. However, since Penrose's (1959) resource-based logic is limited in

explaining unrelated diversification, this conceptual model also draws on dynamic capabilities (Eisenhardt & Martin, 2000) and absorptive capacity (Cohen & Levinthal, 1990).

Dynamic capabilities emphasize that changes to an organization's resources can lead to increasingly unrelated diversification (Eisenhardt & Martin, 2000; Helfat & Raubitschek, 2001; Miller, 2003). Moreover, since unrelated diversification broadens an organization's knowledge base (Eisenhardt & Martin, 2000; Hales, 1999; Miller, 2003), a diverse knowledge base can increase an organization's "absorptive capacity" to assimilate a broader range of market opportunities (Cohen & Levinthal, 1990; Lane, Koka, & Pathak, 2006; Nicholls, Nixon, & Woo, 2003). As new information is assimilated, it promotes new learning, which can increase an organization's absorptive capacity to further diversify into unrelated markets or industries (Bowman & Hurry, 1993; Lane et al., 2006). Thus, physical resources and intangible resources (brands, human skills) can be beneficial for unrelated diversification.

2.6 Related Diversification

Researchers have investigated diversification and firm performance for almost 40 years. Scholars have examined the relationship between diversification and firm performance depending on accounting-based performance and market-based performance. Ramanujam (1987) suggested that related firms outperform unrelated firms, using Standard Industrial Classification (SIC) count categorical classification. The entropy measure of diversification has been used by strategy researchers in response to the need for an objective measure that addresses strategic differences.

Rumelts (1974, 1982) indicated that related diversification produces greater profits than unrelated diversification. In addition, related and unrelated diversification reduces profit volatility. Higgins and Schall (1975), Lewellen (1971), and Schere (1980) suggested that diversified firms can allocate their capital resources more efficiently than undiversified firms by optimally using internal capital. Martin and Sayrk (2003) illustrated that diversification can also mitigate failure in new markets through cross-subsidization regarding the decrease in financial risk.

Some empirical studies have asserted that related diversification increases profits more than unrelated diversification (Barton, 1988; Bettis, 1981; Bettis & Hall, 1982; Lecraw, 1984; Lubatkin & Rogers, 1989; Montgomery & Singh, 1984; Palepu, 1985). Bettis (1981) found that related diversification outperforms unrelated diversification by approximately one to three points of return on assets. Palepu (1985) suggested that profitability growth is significantly larger with related diversification than unrelated diversification. Lubatkin and Rogers (1989) found that related diversification tends to create better market returns than unrelated market diversification.

Generally, related diversification happens when a parent and its subsidiary operate in congruent areas, while unrelated diversification occurs when a parent and its subsidiary operate in dissimilar areas. A restaurant that acquires another restaurant is an example of diversification because the investment is made in firms in various restaurant sectors.

Although advocates of related diversification contended related diversification is better than unrelated diversification in terms of profitability, defenders of unrelated diversification asserted that unrelated diversification had various investment

opportunities (Scharfstein & Stein, 2000). Thus, unrelated diversification can increase profits more than related diversification because of the decreased cost of capital and investment in a better position (Hill & Snell, 1988).

In particular, some researchers found no evidence that related diversification provided more advantages than unrelated diversification (Bass, Cattin, & Wittink, 1978; Chatterjee, 1986; Grinyer & Yasai-Ardekani, 1980; Ravenscraft, 1983). Consequently, the profitable advantage of related diversification is conflicting in terms of its rationale and in empirical studies in terms of resource-based views.

2.7 Tangible and Intangible Resources between Restaurant Segments

An important notion that appears consistently in the resource-based view is heterogeneity in firm resources. These resources may be tangible or intangible and can be classified as physical and human. Homogeneous versus heterogeneous resource distribution has been discussed explicitly by previous researchers who compared the market model of competitive advantage (Porter, 1980) and the resource-based view of the firm (Barney, 1991; Peteraf, 1993).

Tse and Olsen (1988) found that most executives in the limited-service restaurant segment perceived their strategies as primarily low-cost producers. In contrast, most executives in the full-service restaurant segment viewed their strategies as primary differentiation (Harrington, 2011). This suggested more reliance on heterogeneous resources for firms in the full-service restaurant segment. The National Restaurant Association suggested that the limited-service restaurants had relatively higher homogeneous resources for two reasons.

First, marketing costs as a percentage of total sales are consistently higher for limited-services restaurants than for full-service restaurants. This indicates national branding (intangible resource) or marketing efforts that imply more of a focus on the industry as a level of analysis and external differentiation is characteristic of the market model of competition, which assumes homogeneous resources (Peteraf, 1993).

Second, limited-service restaurants appear to lend themselves more readily to standardization, which suggests more operating facilities (tangible resources). In addition, the higher employee turnover rate and nonhuman skills (intangible resources) in the limited-service restaurants suggest that any unique abilities will be more quickly dispersed to other firms in the segment (Decarolis & Deeds, 1999). Thus, full-service and limited-service restaurants are different sectors or segments in terms of the resource-based view such as tangible and intangible resources.

2.8 Financial Resources between Restaurant Segments

The restaurant industry is particularly vulnerable during times of economic distress (Gu, 1993). In general, this industry has lower profit margins than other industries, averaging between 2% and 6% (Skidelsky, 2009), further aggravating the effect a recession has on the industry. Full-service and limited-service restaurants tend to react differently to the recession effect in terms of financial resources.

Full-service restaurants generally rely on high profit margins because sales are mainly derived from customers' discretionary spending. When a recession occurs, customer sentiment and household income are lower, and full-service restaurants are the first to feel the effects (Youn & Gu, 2010). However, fast-food restaurants depend on

large sales volume to compensate for lower profit margins. Sales are primarily necessity expenditures. Limited-service restaurants have steadier revenues (Youn & Gu, 2010) while the liquidity and profitability ratios have generally improved in the postrecession period for full-service restaurants in restaurant sectors. That may mean that when restaurant firms operate in two sectors, the profits may increase more or better than when the parent restaurant firms operate in only the same sector.

Further, Gu (1996) suggested that full-service restaurants had a lower current acid test and operating cash flow to current liability ratios. In comparison, limited-service restaurants had a higher current and acid test ratio and cash flow coverage for current liabilities. Lower liquidity may partly be attributed to full-service restaurants' increased interests because of increased long-term debt financing. Therefore, full-service and limited-service restaurants can be divided into different segments because the different segments have unique financial features in terms of financial resources.

2.9 Types of Acquisition under Study

In this study, the types of acquisitions include same-sector and different-sector acquisitions. When a full-service restaurant acquires a full-service restaurant or a limited-service restaurant acquires a limited-service restaurant, the acquisition is a same-sector acquisition. When a full-service restaurant acquires a limited-service restaurant or limited-service restaurant acquires a full-service restaurant, the acquisition is a different-sector acquisition.

Researchers have used three approaches to measure the difference between related diversification and unrelated diversification: (a) categorical measures, (b) SIC measures,

and (c) resource-based views (Davis & Duhaime, 1992). Categorical measures are built on typological work (Wrigley, 1970) and typically involve classification of a firm in terms of one of several characteristic types of diversification. SICs are the most commonly used determinants in the literature. The resource-based view has been used in situations in which categories are hard to apply or where SIC data are not available, such as when diversification occurs within firm boundaries. Unlike traditional SIC measures, the new concept of relatedness views each industry or line of business as a combination of resources (Farjoun, 1998).

In addition, many scholars have noted the shortcomings of using exclusively SIC-based measures to determine the extent of diversification activities (Wade & Gravill, 2003). In other words, the SIC code was considered along with a measure of diversification experience to determine whether a parent and a subsidiary were related. Consideration of only the parent's SIC code might underestimate the extent of the parent firm's experience in the industry. For example, a parent may operate in one industry, but investment may extensively occur in another sector of the industry. Thus, areas in which the parent firm has experience in another sector of one industry should be measured in terms of the resource-based view. Consequently, diversification within one industry must be determined by relatedness in the sectors or groups in terms of the resources-based view rather than by similarity in the physical attributes of products in the same industry (i.e., the four-digit SIC code).

For instance, the restaurant industry uses 5812 (eating places), and restaurants can be classified as full-service and limited-service restaurants in terms of the North American Industry Classification (NAICS). The NAICS is the standard used by federal

statistical agencies to classify business establishments to collect, analyze, and publish statistical data related to the U.S. business economy. The NAICS was developed under the auspices of the Office of Management and Budget (OMB) and adapted in 1997 to replace the SIC system. In this study, the relevant sectors and the NAICS-based measures correspond empirically.

Full-service and limited-service restaurants make same-sector (i.e., full-service to full-service or limited-service to limited-service) and different-sector (i.e., full-service to limited-service or limited-service to full-service) acquisitions because of similar market profiles and resource endowments. Thus, the main purpose of the experiment in this study is to examine how the financial performance of the acquiring firm is affected and how the operating performance of the acquiring firm is influenced depending on a resource-based view when a segment is extended via acquisition. Consequently, in this study, the terms *different-sector acquisitions* and *same-sector acquisitions* are used.

2.10 Hypotheses

This study addresses a significant knowledge gap by focusing on marketing, financial strategy, and operating perspectives for sectors through the type of acquisition on the effects of particular theoretical importance and managerial interest. Thus, all else being equal, when a firm has a strong management strategy, the firm can generate profits and improve performance due to acquisitions. From this perspective, based on the literature review, in this section hypotheses are proposed.

2.10.1 Performance through Acquisition

Although a few studies investigated the effects of acquisition on restaurant performance, most examined only short-term and long-term abnormal returns by studying M&As. Previous M&A studies of the restaurant industry showed different results regarding whether acquiring firms had positive or negative or not significant abnormal returns in the stock market after acquisitions (Andrew, 1988; Enz, Canina & Walsh, 2001; Hsu & Jang, 2007; Jensen & Ruback, 1983; Kwansa, 1994; Sheel & Nagpal, 2000). However, stock returns may not correlated with a firm's accounting performance because changes in the market valuation around the time of the takeover would not reflect the restaurant firms' accounting performance.

In the hospitality literature, Hsu and Jang (2007) suggested that hotel firms' mergers had a negative effect on ROA and ROE, but the study may not fully explain firms' profitability. The authors compared the means of the ROA and the ROE of 1, 2, and 3 years before the merger and 1, 2, and 3 years after the merger, but the effect of the M&A could occur after the merger. Thus, a firm's performance each year after the merger may need to be compared with 1 year before the merger.

Although no empirical study has investigated the long-term accounting performances of acquiring restaurant firms, theoretical arguments on the benefits of acquisition suggested firms can lead to increased acquisition performance through market power, efficiency, and economies of scale (Butters, Lintner, & Cary, 1951; Dussauge & Mitchell, 1988; Edwards, 1955; Levy & Sarnat, 1970; Lewellen, 1971; Lintner, 1971; McGuckin & Nguyen, 1995;). Similarly, through acquisitions, the restaurants' performance can increase according to the three perspectives.

First, in terms of market power, restaurants can generate company-operated firms and more franchises or increase market share to control food price and production. Further, firms can increase sales growth and firm size through increased equipment and plants that contribute to productivity and reduce costs.

Second, in terms of efficiency, restaurant firms might have a low tolerance for risk and for the potential losses that could be incurred from investing in failed food products and quickly acquire food product skills. In addition, restaurants could make more effective strategic decisions to assemble a portfolio of complementary brands and products because different investment options can provide balance and diversify risk in a securities portfolio.

Third, in terms of economies of scale, restaurant firms can be managed such that there are low barriers to entry and there are a large number of entrepreneurs. Additionally, the firms can broaden their geographical range effectively by adding multiple stores and brands.

However, some empirical studies found acquisitions had a negative effect on firm performance. For example, Singh (1971) suggested two thirds of the surviving companies reported lower profits in the year of the merger and three quarters had lower profitability in the third postmerger year. Dickerson et al. (1997) and Utton (1974) also asserted that postacquisition profitability deteriorated. Utton compared the profitability of a sample of merger-intensive firms with a random sample of firms that grew primarily through internal expansion and argued that average profitability measured by the pretax rate of the return on net book assets was significantly lower for the merging firms than for the control firms.

In addition to firm performance, the link between acquisition and executive compensation was widely investigated in previous studies (Barle & Means, 1932; Baumol, 1959; Core, Holthausen, & Larcker, 1999; Elston & Goldberg, 2003; Finkelstein & Hambrick, 1989; Mangel & Singh, 1993; McKnight, 1996; Mueller, 1969; Williamson, 1975). Executive compensation is one reason that firms make acquisitions. Large public firms need to hire high-quality executives, and they induce higher payments or bonuses for themselves (Agarwal, 1981; Core et al., 1999; Riahi-Belkaoui, 1992). In particular, Kroll, Simons, and Wright (1990) asserted that an increase in firm size achieved through M&As led to significant increases in CEO compensation for owner- and manager-controlled firms. Thus, restaurant firms' acquisitions could be also related to managerial compensation.

In addition, scholars have often argued but researched less often that cultural differences can be a source of confusion, hostility, and distrust between the members of the merging organization (Buono & Bowditch, 1989; Krug & Nigh, 2001; Olie, 1990) and a major contributor to the high failure rates reported in the M&A literature (Datta, Pinches, & Narayanan, 1992; King, Dalton, Daily, & Covin, 2004). Restaurant firms that acquire other firms may find it hard to increase their performance due to cultural differences such as different cultural distance, management style, and cultural fit between acquirers and targets (Chartfield, Dalbor, & Ramdeen, 2011).

In general, most restaurants are small businesses. Seventy percent have fewer than 20 employees, and more than 70% of restaurants are single-unit (independent) operations (Chatfield et al., 2011). In recent years, the restaurant industry has experienced tremendous competition (Gu, 2002), and many restaurants failed due to rapid expansion

through M&As (Schwartz, 1999). Gu (2002) suggested that the restaurant industry had more business failures than any other industry that saw numerous M&As.

In terms of the theoretical advantages of M&A, the market power of restaurant firms may be limited because food is not a high-technology product whose prices can be controlled in the market. The price of food, depending on the menu, is generally consistent in the restaurant industry. Further, the efficiency of restaurant firms can be lower than other industries such as manufacturing and technology firms. Restaurants cannot effectively use or save food inventory for a long time because food is perishable. Of course, this study does not claim that market power, efficiency, economies of scale, compensation, and cultural differences are not necessary casual factors that contribute to the success and failure of restaurant acquisitions. Numerous variables have been proposed that influence the accounting performance of restaurant firms that engage in acquisition activity. Nevertheless, the theoretical benefits of M&As are weaker for restaurant firms compared to other industries because of the food and service industry. Consequently, the following was hypothesized:

H₁: Acquisitions have negative effects on restaurants' performance over the long term.

2.10.2 Different-Sector Acquisition vs. Same-Sector Acquisition

Although a range of costs may increase during acquisitions, the data suggest that, in general, acquisitions are meant to maximize a firm's value (Salter & Weinhold, 1979). The dominant theory related to how this value can be created suggests that firms acquire other firms with related resource-based views, thus creating efficiency through synergy.

Synergy may imply that gains accrue to the acquiring firm through three sources: (a) improved operating efficiency, and plant, property, and equipment (PPE) based on physical resources; (b) some type of assets of brand and human skill transfer based on intangible assets; and (c) revenue, liquidity, and leverage based on financial resources. Some scholars have suggested that synergistic efficiencies generate market power over competitors (Bradley, Desai, & Kim, 1983; Eckbo, 1983; Montgomery, 1985; Stewart, Harris, & Carleton, 1984).

Traditional diversification scholars have argued that similarities among acquiring and target firms' resources should lead to higher performance. Although a few hospitality scholars have suggested acquisitions had negative effects on firm performance, resource-based view theory led to the conclusion that complementarity could be more important (Harrison, Hitt, Hoskisson, & Ireland, 2001). For example, full-service and limited-service restaurants have advantages and disadvantages with different resource features in terms of the resource-based view. Each restaurant sector's unique resources can be realized by integrating complementary resources through acquisitions. Complementing resources by different-sector acquisitions could provide more opportunity for the restaurants to create competitive advantages that could be sustained for a longer period of time than same-sector acquisitions because different-sector acquisitions could strengthen their advantageous resources and make up for their weak resources by complementing resources through acquisitions. Thus, the effects of acquisition on restaurant firms' performance could be different depending on how each sector's resources is combined.

Of course, same-sector acquisitions with highly similar resources may be able to achieve greater market power and to promote redeployment of assets. However, same-

sector acquisitions may not be able to develop other valuable potential synergies as a result of their integration because of the limitation of using various resources. In contrast, integrating different yet complementary resources between different-sector acquisitions may present more opportunities for synergy derived from tangible, intangible, and financial resources.

Barney's (1988) proposition that synergy may be a necessary but not in sufficient condition to gain value for the acquiring firm may offer insight if a related acquisition or an unrelated acquisition produces more value. Barney (1988) suggested that value is created for the acquiring firm when private and uniquely valuable cash flows exist between the acquiring and target firms. Unique resources exist when an acquiring restaurant firm will benefit more than another acquiring firm from the synergy created through acquisition. Harrison et al. (2001) investigated combining resources through acquisitions, using a sample of approximately 400 acquisitions, to assess resource similarity versus complementarity. The authors suggested that resource complementarity creates the potential for greater synergy from acquisitions, leading to higher long-term firm performance as an end result.

In addition, a resource-based perspective of firm strategy (Wernerfelt, 1984) suggested that merged firms with high similarity and relatively different resource integration in critical areas could be expected to enjoy great performance improvements compared to merged firms with widely disparate resource distributions. Acquisitions of target firms with operating and corporate strategic resources for the acquiring firm are expected to produce significant synergies because the financial performance improves. However, aspects of synergy (physical resources, brand names, human skills, and funds)

may imply an appropriate combination of tangible, intangible, and financial resources with different resources between acquiring and target restaurants as the source of knowledge for value creation. Different resources could be more positively associated with resource complementarity in the different-sector acquisitions.

Thus, resource complementarity provides a rich base for the study of synergy between acquiring and target restaurants and the associated performance outcomes that result from acquisitions. The approach for the resource-based view of the firm could be more complementary than the traditional division between related and unrelated diversification because this study focuses on specific resource perspectives.

In the global economy, the most successful combined firms rely on complementary resources with different resources as the foundation needed to exploit entrepreneurial opportunities (Ireland, Hitt, Camp, & Sexton, 2001). This can be applied to restaurant firms because different resources combined can suggest stronger synergies for the development, cost savings, use of equipment, and financial structure.

Additionally, different resources for full-service restaurants and limited-service restaurants in terms of capital investments likely result in relatively high degrees of variance in the types of capital equipment used and the types of skills that employees possess. Full-service restaurants may acquire limited-service restaurants to extend economic scope, save labor costs, and use more debt financing. Such synergy may help the acquiring firm respond more quickly to competitors' economic scale. Integrating two sets of different but complementary resources and capabilities allows firms to develop and take advantage of new opportunities (Hitt, Bierman, Shimizu, & Kochhar, 2001). Consequently, if the expertise combines the benefits of resources, the firms could

participate in all types of restaurant sectors because the restaurants could be more effectively managed for financial fluctuations and operating systems.

However, same-sector acquisitions can be risky or less profitable than different-sector acquisitions because the restaurants cannot be more effectively managed with similar resources for financial fluctuation, recession, and food flexibility. Same-sector acquisitions do not necessarily imply a lack of synergy, especially if the synergy is considered private. Barney (1988) asserted that above-normal returns can be generated for the acquiring firm in combination with the target firm if the synergistic relationship is unique for other acquiring firms. An acquiring firm with private synergy based on similar resource patterns is likely to have an advantage because other potential acquirers may not recognize or have the private synergy involved and, therefore, will not enter the auction. If differences are involved and the synergy is private, the degree of similar resources may not be immaterial between the sectors in the restaurant industry: However, private synergy is unusual in the restaurant industry because food and service firms rather than manufacturing or IT firms are involved. Thus, synergy from these similarities may be difficult for other acquirers to optimize and use; thus, they may offer fewer competitive advantages and more limited access in same-sector acquisitions in the restaurant industry.

In contrast, Hitt and Ireland (1986, 1985) found that firms may develop multiple distinctive competencies. Because of the combined competencies, merging two firms may create value that overcomes and controls weakness in one or both acquisition partners. In terms of the resource-based view, restaurants may acquire targets to be more attractive in different markets as well as efficient in the products and distribution of the different resources in the sectors. Consequently, different-sector acquisitions can

effectively integrate and manage resources in order to use the combined benefits while same-sector acquisitions cannot adequately cope in the market. Thus, the relationship between different-sector and same-sector acquisitions was hypothesized.

H₂: Different-sector acquisitions are better than same-sector acquisitions for restaurant performance.

CHAPTER 3. METHODOLOGY

3.1 Long-Term Accounting Performance

Most researchers investigating mergers and acquisitions have taken a short-term view of the topic. Various measures have been used to evaluate the success of acquisitions. These include subjective evaluation (Kitching, 1967; Power, 1982), capital asset pricing measures (Elgers & Clark, 1980), and profitability measures (Dickerson, Gibson, & Tsakalotes, 1997; Kusewitt, 1985; Poindexter, 1970).

3.1.1 Accounting Performance Measure: ROA and ROE

Measures for average quarterly ROA and average quarterly ROE were calculated. These measures allowed us to compare differences in the productivity of the assets and owners' equity. Although accounting measures have their shortcomings, ROA is one of the more robust accounting-based measures of economic performance (Brealey & Myers, 1984). ROE provides an accounting-based measure of performance that includes the effects of financial leverage. Some studies have shown that the best strategy for maximizing profitability is not necessarily the best for maximizing growth (Reid, 1968; Rumelt, 1974).

First, ROA was computed by dividing net income by average total assets for each firm. The average ROA with the quarterly data for a specific year period (e.g., 1 year before, post 1 year, post 2 year, post 3 year, post 4 year, post 5 year) was calculated to

calculate the average ROA growth rate change for a specific period. Each average ROA growth rate change for a specific period was calculated by comparing the prior 1 year for each year (e.g., prior 1 year vs. post 1 year, prior 1 year vs. post 2 year, prior 1 year vs. post 3 year, prior 1 year vs. post 4 year, prior 1 year vs. post 5 year). An accounting-based measure cannot be used to isolate the effects of an acquisition event. Biggadike (1979) and Lubatkin (1983) asserted that an acquisition did not affect profitability for at least several years. Thus, the effect for a specific period such as 5 years was studied.

Second, ROE was calculated by dividing net income by average stockholder equity for each firm. Each average ROE growth rate change was calculated with the same method for the average ROA growth rate change calculated. The change in the average growth rates for a specific period was calculated as the same method for the average ROA growth rate change and the average ROE growth rate change.

3.1.2 Control Variables for Long-Term Accounting Performance

Revenue is used as a control variable instead of a measurement of size in this study. Many general financial economics studies use total assets to proxy a firm's size (Lang, Stulz, & Walkling, 1991). However, since franchising through acquisitions, a widely adopted growth strategy in the restaurant industry (Lee, Singal, & Kang, 2013), is prevalent, total revenues that include franchise fees more appropriately reflect a restaurant firm's size than total assets. Therefore, revenue was included as a control variable.

Leverage shows the debt-to-assets ratio (total debt divided by total assets) and controls for the effect driven by a firm-specific capital structure. Higher leverage enables

a firm to take advantage of tax shields due to the deduction of interest expense, which is helpful for increased cash flow and a higher Tobin's Q (McConnell & Servaes, 1990). However, when a firm has excessive debt, the firm's equity return may decrease due to the perception of risk in the market (Brealey & Myers, 2003). Thus, leverage was included as a control variable.

Jensen and Ruback (1983) suggested that liquidity is related to risk because high liquidity could result in agency costs with high free cash flows. High liquidity may not be efficiently invested for available resources, which may accumulate more risk (Borde, 1998). Additionally, Chatterjee and Wernerfelt (1991) asserted that managers may have an incentive to increase the level of diversification to decrease risk with high free cash flows. In this study, liquidity was measured with the log of quick ratio (sum of cash, marketable securities, and accounts receivable to current liabilities).

Property, plant, and equipment (PP&E) was measured as a control variable to study investment opportunities in firms (Demsetz & Villalonga, 2001) because PP&E means that a firm is usually characterized by profitable investment opportunities and invests in them. Thus, PP&E was likely to be related to firm performance in explaining firms' profitability. This variable was calculated as the log ratio of property, plants, and equipment to total assets. For the control variables, the year the acquisition occurred was used.

3.2 The Wilcoxon Rank Transformation

Many nonparametric methods as parametric methods applied to transformed data. The Wilcoxon rank test was used because the observations included 30 firms. This test

makes the results understandable and reasonable. This approach is a class of nonparametric methods. The rank transformation approach also provides a useful method in multiple regression, discriminant analysis, cluster analysis, analysis of experimental designs, and multiple comparisons.

The rank transformation approach provides a useful pedagogical technique for introducing nonparametric methods as an integral. Therefore, the Wilcoxon rank-sum test and the Wilcoxon signed-rank test were used to identify statistically significant differences between the full-service and limited-service restaurant sectors with z tests.

3.3 Models

To measure accounting performance, the regression model included the sum of two variables: average ROA growth rate change and average ROE growth rate change. In this study, the goal was to compare the two sectors. The variance of firms within different-sector and same-sector acquisitions is controlled by introducing control variables. As independent variables, control variables were used to use the entire sample because the constant term indicates the effect of the acquisition by using a regression model. In the study, dummy variables were also used for the type of restaurant acquisition in terms of different-sector and same-sector acquisitions (e.g., different-sector acquisitions: limited-service restaurants–full-service restaurants, or full-service restaurants–limited-service restaurants, same-sector acquisitions: limited-service restaurants–limited-service restaurants and full-service restaurants–full-service restaurants). As control variables, firm revenue, firm leverage, firm liquidity, and firm PP&E were used.

For testing Hypothesis 1, ROA and ROE were calculated using net income as a percentage of the average total assets and net income as a percentage of the average common stock equity, respectively. The postacquisition performance of acquiring firms was compared with their performance 1 year before the acquisition. The average performance for a certain period (e.g., 1 year, 2 years, 3 years, 4 years, and 5 years postacquisition) after the acquisition was compared with the corresponding average performance in the all firms as well as between two sectors using paired z tests. The Wilcoxon rank test is more conservative than a t test, and it is less likely to result in statistically significant differences between preacquisition performance and postacquisition performance changes.

In addition, for testing Hypothesis 2, one equation measured the effect of the acquisition using the entire sample ($t = \text{year}$) among the average ROA growth rate change, the average ROE growth rate change, and the control variables based on acquisitions in the two sectors. The constant term indicated the effect of the acquisition in each sector. The accounting performance changes were measured with a metric with dependent variables in the linear regression.

Additionally, for testing Hypothesis 2, equations 3.1 and 3.2 tested the effect of acquisitions for different-sector and same-sector acquisitions to study which acquisition was more statistically significant. A dummy represented different-sector (as a reference) acquisitions that took 1 if there were same-sector acquisitions and took 0. A positive and significant coefficient of the dummy variable indicates that the different-sector acquisition was better than the same-sector acquisition. The models are as follows:

$$\Delta ROAs_t = \alpha + \beta_1 \text{ dummy} + \beta_2 \text{Revenue}_t + \beta_3 \text{Leverage}_t + \beta_4 \text{Liquidity}_t + \beta_5 \text{PPE}_t + \varepsilon_t \quad (3.1)$$

$$\Delta ROEs_t = \alpha + \beta_1 \text{ dummy} + \beta_2 \text{Revenue}_t + \beta_3 \text{Leverage}_t + \beta_4 \text{Liquidity}_t + \beta_5 \text{PPE}_t + \varepsilon_t \quad (3.2)$$

Last, the effects of the acquisition on different-sector and same-sector acquisitions were measured to study which acquisition was more statistically significant.

3.4 Data Collection Procedures

The sample for this study consisted of publicly traded U.S. restaurant firms. The data used in this study were collected from COMPUSTAT and SDC Platinum using SIC 5812 (eating places) and then divided by the NAICS codes for limited-service restaurants (722211 for the years before 2011 and 722513 for the years after 2011) and full-service restaurants (722110, 722511). There were 54 public full-service restaurants and 14 public limited-service restaurants in the United States. The data matched the COMPUSTAT data.

On SDC Platinum, 96 firms that had acquired other firms were found. Acquiring firms that were private firms, were not listed in the Center for Research in Security Prices (CRSP) database, or did not present information for stock prices per acquiring firm or duplicate firms based on ticker or not parent firms for acquirers were excluded from this sample. Finally, the sample consisted of 30 acquiring firms. The sample covered fiscal years 1992 to 2012. The following three steps were used to measure the firms'

performances for the effects of acquisition. The average ROA growth rate change and the average ROE growth rate change were investigated to measure the effect of acquisitions on the firms' accounting performances. In the following section, the results are discussed.

CHAPTER 4. RESULTS

4.1 Sample Profile

Based on the firms' major service features, the sample was divided into two sectors, full-service restaurants (20 firms) and limited-service restaurants (10 firms). In Table 4-1, details of the acquisitions are listed.

In Table 4-2, the descriptive statistics of accounting performance (ROA and ROE) and the control variables (revenue, leverage, liquidity, and PP&E) of all companies and then of full-service and limited-service restaurants in two sectors from an index for the 20-year period from 1992 through 2012 are summarized. Table 4-2 shows that ROA is significantly positive for all acquiring restaurant firms in the means of the first, second, and fifth years after acquisitions. However, there is no difference between the full-service and limited-service restaurants. In ROE, the mean of the second year after the acquisitions is significantly positive for all acquiring restaurant firms. In addition, the value of the first year is higher in limited-service restaurants than in full-service restaurants.

Revenue, leverage, liquidity, and PPE are the status in the event quarter of acquisitions. Revenue and liquidity are higher in limited-service restaurants than in full-service restaurants. However, PPE is higher in full-service restaurants than in limited-service restaurants. Leverage is not significant between two sectors.

Table 4-3 gives the results of the Wilcoxon sum tests for after the acquisitions on firm performance. For ROA, the mean of the fifth year after the acquisitions is significantly lower in different-sector acquisitions than in same-sector acquisitions. For ROE, the means of the fourth and fifth years after the acquisitions is significantly lower in different-sector acquisitions. The result for the accounting performances was almost the same for all years. In addition, PPE was higher in the same-sector acquisitions than in the different-sector acquisitions in terms of the status in the event quarter of acquisitions.

Table 4.1. A List of Sample Restaurant Firms Created with Acquisitions

Full-service restaurants (20 firms)	Acquired companies	Acquisition announcement date	Limited-service restaurants (10 firms)	Acquired companies	Acquisition announcement date	
Advantica Restaurant Group, Inc	Perk Development Corp (Perkins)	02/05/1999	AFC Enterprises, Inc.	Shelton Development Company (Popeyes Chicken & Biscuits)	05/02/2006	
Benihana, Inc.	Rudy's Restaurant Group	07/23/1997	Biglari Holdings, Inc.	Cracker Barrel Old Country	02/17/2012	
	Ra Sushi Bar restaurant	12/04/2002				
	Teppanyaki Restaurant	09/26/2006				
Bob Evans Farms, Inc.	Haru Holding Corp.	03/08/2010	Burger King Holdings, Inc.	Heartland Food Corp Restaurant	04/30/2008	
	Mimis Cafe	06/14/2004			07/17/2008	
Brinker International, Inc.	On The Border Cafes Inc.	01/24/1994	CEC Entertainment, Inc.	Chuck E Cheese Restaurant	12/22/1998	
	Northwest Restaurant	05/05/1994			Showbiz Pizza Time Inc.	09/09/1997
	Maggiano's Little Italy and Corner Bakery	07/20/1995				
	NE Restaurant Co Inc.	11/20/2000				
	Sydran Group LLC	09/06/2001				
Buca, Inc.	Vinny Testas Restaurants	12/17/2001	CKE Restaurants, Inc.	Summit Family Restaurant	12/01/1995	
Buffalo Wild Wings, Inc.	Avado Brands (Don Pablos)	12/20/2007	Jack In The Box, Inc.	Qdoba Restaurant Corp	01/21/2003	
Cracker Barrel Old City, Inc.	Schapp's Enterprises LLC	12/21/2012	McDonald Corp.	Hardees Food (Roy Rogers Restaurant)	08/02/1996	
	Logans Roadhouse Inc	12/11/1998			World Foods	02/10/1998
					Donatos Pizza	05/06/1999

Table 4-1 (Cont.)

Full-service restaurants (20 firms)	Acquired companies	Acquisition announcement date	Limited-service restaurants (10 firms)	Acquired companies	Acquisition announcement date
Darden Restaurants, Inc.	Quality Dining Inc. (Grady's)	01/16/2002	Nathans Famous, Inc.	Miami Subs Corp	11/30/1998
	Chevy's Rio Bravo Restaurants	08/01/2003		Kenny Rogers Roasters	12/23/1998
	RARE Hospitality Intl Inc.	08/16/2007			
Famous Daves of American, Inc.	North Country BBQ Restaurant	12/18/2009	Panera Bread, Inc.	Bakery Cafes	06/21/2007
Flanigans Enterprises, Inc.	Dannys Restaurant	08/08/1997	Papa Bello Enterprises Inc	Mama's Direct Inc	01/04/2012
Frisch's Restaurants, Inc.	Big Boy Restaurant	09/27/2006			
Granite City Food & Brewery, Inc.	Cadillac Ranch Restaurant	11/04/2011			
Landrys Restaurants, Inc.	CA Muer Corp.	02/19/2002			
	Chart House Restaurants	05/20/2002			
	Saltgrass Steak House	09/11/2002			
	Schussler Creative (T- Rex)	02/27/2006			
Lubys, Inc.	Smith & Wollensky	01/16/2007			
	Triangle Foodservice Wyatt's	07/15/1996			
Mexican Restaurant, Inc.	Fuddruckers Inc.	06/18/2010			
	Casa Ole, Crazy Jose Restaurant	09/26/2003			
	Mission Burritos	08/17/2006			

Table 4-1 (Cont.)

Full-service restaurants (20 firms)	Acquired companies	Acquisition announcement date	Limited-service restaurants (10 firms)	Acquired companies	Acquisition announcement date
O Charleys, Inc.	Burbet Foods	11/03/1993			
	Shoex Inc.	10/11/1995			
	J Alexander's Corp.	04/06/1999			
	Stoney River Legendary	05/03/2000			
	Ninety Nine Restaurant	10/28/2002			
PF Changs Bistro, Inc.	True Food Kitchen	02/16/2012			
Red Robin Gourmet, Inc.	Great Western Dining	03/07/2006			
	Top Robin Ventures	01/31/2007			
	Dane Country Robins Inc.	01/31/2008			
Ruby Tuesday, Inc.	Lime Fresh Mexican Grill	04/09/2012			
Star Buffet, Inc.	K-Bob's USA Restaurant	02/01/2006			
	Pecos Diamond Steakhouse	07/11/2006			
	Western Sizzlin Franchised Restaurant	11/10/2006			
	Whistle Junction Buffet Restaurant	11/28/2006			
	Holiday House Restaurant	05/04/2007			
	Bar H Steakhouse	06/05/2007			
	Rankin Bros Inc.	06/20/2007			
	4Bs Restaurant	07/31/2007			
	JJ North's Grand Buffet	10/19/2007			

Table 4.2. Descriptive Statistics of Firm Performance for the Entire Sample in the Two Sectors (over 1992–2012)

	All Companies		t value	Full-Service Restaurants (a)		Limited-Service Restaurants (b)		H ₀ : a=b
	Mean	Std Dev		Mean	Std Dev	Mean	Std Dev	
1 st yr ROA ^c	0.051	0.064	6.272***	0.044	0.051	0.070	0.091	-1.385
2 nd yr ROA	0.052	0.058	6.891***	0.046	0.054	0.071	0.066	-1.376
3 rd yr ROA	0.019	0.127	1.143	0.005	0.138	0.064	0.072	-1.540
4 th yr ROA	0.006	0.154	0.271	0.000	0.149	0.022	0.171	-0.469
5 th yr ROA	0.033	0.106	2.077**	0.024	0.109	0.057	0.094	-0.900
1 st yr ROE ^d	0.241	1.644	1.154	0.018	0.462	0.881	3.124	-1.843*
2 nd yr ROE	0.090	0.132	5.169***	0.086	0.104	0.101	0.199	-0.369
3 rd yr ROE	-0.031	0.493	-0.477	-0.074	0.552	0.099	0.186	-1.145
4 th yr ROE	0.373	3.058	0.871	0.548	3.578	-0.090	0.457	0.662
5 th yr ROE	0.053	0.963	0.369	-0.075	0.889	0.404	1.109	-1.492
Revenue	379.894	683.541	4.341***	239.444	353.102	810.609	1156.747	-2.991***
Leverage	0.224	0.151	11.574***	0.217	0.143	0.244	0.176	-0.588
Liquidity	0.428	0.538	6.218***	0.298	0.391	0.830	0.720	-3.654***
PPE	0.727	0.171	33.100***	0.776	0.109	0.577	0.235	4.490***

Note: ROA= rate of return on assets; ROE = rate of return on common stock equity. 1st yr ROA^c = first year ROA after an acquisition; 1st yr ROE^d = first year ROE after an acquisition.

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

Table 4.3 The Wilcoxon Rank-Sum Tests for Postacquisition on Firm Performance

	Different-Sector Acquisitions (a)		Same-Sector Acquisitions (b)		H ₀ : a=b Z
	Mean	Std Dev	Mean	Std Dev	
1 st yr ROA ^c	0.034	0.090	0.057	0.051	-0.780
2 nd yr ROA	0.044	0.074	0.055	0.052	-1.389
3 rd yr ROA	0.034	0.082	0.015	0.138	0.190
4 th yr ROA	0.007	0.131	0.006	0.162	-0.655
5 th yr ROA	-0.011	0.105	0.047	0.103	-1.757*
1 st yr ROE ^d	0.879	3.117	0.019	0.479	0.088
2 nd yr ROE	0.108	0.116	0.084	0.136	-0.354
3 rd yr ROE	0.094	0.131	-0.068	0.552	0.761
4 th yr ROE	-0.020	0.207	0.494	3.497	-1.654*
5 th yr ROE	-0.021	0.229	0.077	1.104	-1.704*
Revenue	202.804	272.040	442.860	772.296	-0.623
Leverage	0.219	0.174	0.225	0.144	-0.246
Liquidity	0.681	0.822	0.339	0.364	1.304
PPE	0.630	0.207	0.762	0.143	-2.140**

Note: ROA= rate of return on assets; ROE = rate of return on common stock equity. 1st yr ROA^c = first year ROA after an acquisition; 1st yr ROE^d = first year ROE after an acquisition.

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

4.2 Testing Hypothesis 1

In Table 4-4, the results of the Wilcoxon signed-rank test for postacquisition ROA and ROE changes up to 5 years are shown; there are significant negative effects.

However, the negative effects are the strongest within a year after acquisition and decreased until 4 years compared with the previous year. After 4 years, the negative effects turn to positive compared to the previous year in ROA and ROE changes.

Consequently, the results demonstrate that acquiring restaurant firms' market performance is significantly negative on accounting performance. As a result, Hypothesis 1 was not supported.

Table 4.4. The Wilcoxon Signed Ranks Tests for Postacquisition Accounting Performance Change

	All Acquisition		Different-Sector Acquisitions (a)		Same-Sector Acquisitions (b)		H ₀ : a=b
	Mean	Z	Mean	Z	Mean	Z	Z
Panel A: ROA							
1 st yr post - base yr	-0.022	-2.409**	-0.060	-1.710*	-0.009	-1.743*	-0.788
2 nd yr post - base yr	-0.023	-2.667***	-0.056	-1.363	-0.014	-2.218**	-0.746
3 rd yr post - base yr	-0.058	-3.961***	-0.066	-1.223	-0.056	-3.834***	0.666
4 th yr post - base yr	-0.083	-4.879***	-0.114	-2.824***	-0.074	-3.957***	-1.299
5 th yr post - base yr	-0.063	-4.442***	-0.140	-2.756***	-0.038	-3.480***	-1.928*
Panel B: ROE							
1 st yr post - base yr	0.080	-2.468**	0.513	-1.086	-0.070	-2.185**	-0.072
2 nd yr post - base yr	-0.093	-2.799***	-0.312	-1.992**	-0.030	-2.139**	-0.858
3 rd yr post - base yr	-0.218	-3.734***	-0.325	-1.223	-0.186	-3.600***	0.390
4 th yr post - base yr	0.161	-4.106***	-0.488	-2.746***	0.361	-3.098***	-1.921*
5 th yr post - base yr	-0.171	-3.257***	-0.524	-2.490**	-0.057	-2.214**	-2.021**

Note: ROA= rate of return on assets; ROE = rate of return on common stock equity.

1st yr post^a = first year ROA after an acquisition, base yr^b = 1 year ROA before an acquisition; 1st yr post^c = first year ROE after an acquisition, base yr^d = 1 year ROE before an acquisition.

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

4.3 Testing Hypothesis 2

Table 4-4 shows that the results of the Wilcoxon signed-rank test. The results indicate that there is no significant difference in postacquiring firm performance between same-sector and different-sector acquisitions.

Tables 4-5 and 4-6 show the regression results for the firms' accounting performances for acquisitions in different sectors and in the same sector. The results show that there is no significance between different-sector and same-sector acquisitions for all periods. However, the ROE of different-sector acquisitions is significantly positive in only the first year. In addition, leverage had a significant negative impact on the ROA and the ROE growth changes in all years except the fourth year. Consequently, there is

no significance between different-sector and same-sector acquisitions. Thus, Hypothesis 2 is not supported.

Table 4.5 Results for ROA Changes in Different-Sector and Same-Sector Acquisitions

	1st year	2nd year	3rd year	4th year	5th year
	ΔROA^a	ΔROA	ΔROA	ΔROA	ΔROA
Different sector ^b	-0.157 (0.098)	-0.078 (0.095)	-0.102 (0.136)	-0.253 (0.151)	-0.324 (0.138)
Same sector ^c	0.028 (0.034)	0.017 (0.031)	-0.026 (0.044)	-0.028 (0.049)	0.038 (0.044)
Revenue	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
Leverage	-0.202** (0.099)	-0.236** (0.102)	-0.389** (0.146)	-0.120 (0.175)	-0.318* (0.158)
Liquidity	0.021 (0.037)	-0.016 (0.037)	-0.001 (0.053)	-0.027 (0.058)	0.058 (0.050)
PP&E	0.199* (0.114)	0.124 (0.104)	0.175 (0.149)	0.281* (0.157)	0.336** (0.156)
Adj. R^2	0.081	0.104	0.120	0.134	0.245
F value	2.050*	2.300*	2.500**	2.510**	3.790***
N	61	57	56	50	44

Note: ROA= rate of return on assets. ^a1st year ΔROA = first year ROA after an acquisition – 1 year ROA before an acquisition. ^bDifferent sector stands for dummy =1 as different-sector acquisitions. ^cSame sector stands for dummy = 0 as same-sector acquisitions

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$.

Table 4.6 Results for ROE Changes in Different-Sector and Same-Sector Acquisitions

	1st year	2nd year	3rd year	4th year	5th year
	ΔROE^a	ΔROE	ΔROE	ΔROE	ΔROE
Different sector ^b	2.220** (0.956)	-0.605 (0.457)	-0.574 (0.621)	-0.272 (3.677)	-1.825 (1.071)
Same sector ^c	-0.365 (0.333)	0.165 (0.146)	-0.017 (0.199)	0.792 (1.184)	-0.118 (0.344)
Revenue	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)	0.000 (0.000)
Leverage	1.636* (0.965)	-1.464*** (0.488)	-2.186*** (0.667)	-0.429 (4.258)	-2.593** (1.223)
Liquidity	-0.442 (0.356)	0.023 (0.179)	0.061 (0.243)	-0.492 (1.413)	0.389 (0.391)
PP&E	-2.813** (1.103)	0.914* (0.498)	1.007 (0.676)	0.422 (3.817)	2.526** (1.213)
Adj. R^2	0.127	0.222	0.197	-0.082	0.170
F value	2.750**	4.200***	3.710***	0.260	2.770**
N	61	57	56	50	44

Note: ROE= rate of return on common stock equity. ^{1st year} ΔROE = first year ROE after an acquisition – 1 year ROE before an acquisition. ^bDifferent sector stands for dummy =1 as different-sector acquisitions.

^cSame sector stands for dummy = 0 as same-sector acquisitions

* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$.

CHAPTER 5. CONCLUSION

5.1 Key Findings

In this study, the overall acquisition effects of restaurant firms were significantly negative on the firm's ROA and ROE. The results of the Wilcoxon signed-rank test for postacquisition ROA and ROE changes up to 5 years showed significant negative effects. However, the negative effects were strongest within a year after the acquisition occurred and decreased until 4 years later compared with the previous year. After 4 years, the negative effects turned positive compared to the previous year in the ROA and ROE changes. These results indicate that acquiring firms cannot recover fully from the negative impacts after acquisition but the negative impacts become fainter as the years go by.

The other findings are that even though there is no significant difference in postacquiring firm performance between same-sector and different-sector acquisitions, the overall z scores of different-sector acquisitions from the Wilcoxon rank tests show less negative postacquisition performance than same-sector acquisitions in ROA and ROE changes. The ROA changes in 2 and 3 years and the ROE changes in 1 and 3 years after acquisitions even appear nonsignificant only for the different-sector acquisitions. The results imply that different-sector acquisitions are less negative than same-sector

acquisitions. However, neither the results of the Wilcoxon rank tests nor regression analysis reveal significant differences in firm performance between the two types of acquisitions. Therefore, the effects of acquisition for different-sector and same-sector acquisitions are negative, and there is no significant difference between them.

5.2 Theoretical Implications

The findings of this study provide a perspective on the effect of acquisitions on firm performance. Most hospitality scholars have revealed that M&As are not beneficial for the acquiring firms' performance or do not, at the minimum, last short-term. This study is in line with earlier studies that showed negative postacquisition operational performance but differs from the previous findings in terms of year effects since the negative effects are diminished after acquisition.

Additionally, in this study a resource-based view of restaurant segmentation was applied as a motivation for acquiring restaurants. This attempt is still meaningful because the relatedness of the business is a critical success factor (Canina et al., 2010) when restaurant managers consider acquiring other firms. Most previous studies investigated financial performance using combined restaurant firms' data. The researchers did not classify sectors in the same industry or identify public and private firms. Thus, this study helps broaden understanding of restaurant firms' postacquiring performance by differentiating full-service and limited-service restaurants in complicated acquiring procedures even though the results have not proposed sufficient theoretical support regarding the effect of acquisitions in the restaurant industry.

5.3 Managerial Implications

From a practical viewpoint, the results suggest that acquiring other firms as a growth strategy is not appropriate for restaurant firms' future profitability. In addition, since the negative acquisition effects last for more than 4 years, the restaurant firms should have enough financial capacity to overcome the deteriorated firm performance. Therefore, managers of the acquiring firm must consider their own market position, financial condition, human resources, and future economic environment with a long-term view when they plan to acquire other firms.

The results of this study cautiously suggest that different-sector acquisitions may be more beneficial than same-sector acquisition even though both types of transactions led to negative accounting performances for up to 5 years. Therefore, if restaurant firms need to grow faster for any strategic reason in spite of sacrificing their profit, they should acquire restaurants in different sectors. In addition, this study implies that due diligence procedures, deal types, and valuation of target firms are important; managers should deliberately include bargaining factors during the deal negotiation process.

5.4 Research Limitations

This study is not free from limitations. First, the sample size is small. The results may not be able to be generalized to other hospitality industries. Second, several important factors such as the type of payment, dividends, stock splits, and the degree of acquisition experience were not controlled in this study. Third, the debt situation when restaurants made acquisitions was not considered. Thus, the effects of the acquisitions may not have been clearly confirmed.

Future studies should consider these limitations to advance understanding of acquisitions by comparing various financing resources that may affect restaurant performance after acquisitions in each sector in the restaurant industry. Such an investigation would help restaurant executives find methods for positive abnormal returns and significant profitability as well, thus improving their performance in terms of ROA and ROE. Nevertheless, the results suggest that different types of acquisitions influence restaurant firms' performance differently.

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