Harvard Business Review

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Why Fusing Company Identities Can Add Value

M&A by Jonathan Knowles, Isaac Dinner, and Natalie Mizik

Among financial researchers, it's well established that newly merged companies usually underperform the market. There's an infrequent but important exception, though: Corporations that brand themselves with a "fusion" of the merging companies' identities typically enjoy higher returns.

We studied 216 companies formed by large mergers that took place from 1997 to 2006. First we divided them into three groups on the basis of their corporate branding strategies. "Assimilation" includes organizations that retained the name and logo of one of the original companies and discarded those of the other, as Pfizer did when it took over Warner-Lambert. "Business as usual" denotes instances in which each firm kept its name and logo: This was the case when Procter & Gamble bought Gillette. "Fusion" describes organizations that used branding elements from both companies, either by combining the two names (as in JPMorgan Chase) or by taking the name of one company and the logo of the other (Boeing kept its name but adopted McDonnell Douglas's logo). Although some merging companies opt for an entirely new name (as GTE and Bell Atlantic did when they joined to form Verizon), this strategy is so rare that it could not be separately evaluated.

Then we analyzed the performance of each company's stock from the date of the deal's closing to three years after the merger was complete, and calculated the average return for each of the three groups relative to the market as a whole. After adjusting for such factors as risk, size, and market-to-book ratio, we found that companies using an assimilation branding strategy fell short of the market return by 15%, on average, and companies using a business-as-usual strategy fell short by 25%—but companies using a fusion strategy exceeded the market return by 3%.

Our results indicate that there may be hidden costs to the more expedient assimilation and business-as-usual approaches—the approaches used in most mergers. Because a merger's success relies in part on preserving positive feelings among customers and employees, it's smart to pursue a branding strategy that explicitly seeks to transfer equity from both merging companies to the new one. This is true even though fusing two companies' identities may be cumbersome and expensive.

As the economy improves, the number of mergers is rising, as are managers' concerns about the dismal stock performance typically achieved by newly combined companies. Using a fusion strategy to send reassuring signals to customers and employees—and, ultimately, investors—may increase the chance of a successful deal.

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