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MERGER & ACQUISITION IN THE INDIAN CONTEXT: THE IMPACT ON SHAREHOLDER VALUE

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ABSTRACT

One of the primary motives behind any strategic corporate decision is to maximize shareholder value. Strategic decisions for firms are made with the objective of maximizing the wealth of the company's shareholders. This paper investigates the performance of selective sector of chemical companies, which have been involved in chemical related mergers and acquisitions and examines the impact of merger announcements on acquiring firms' and target firms' stock performance in the Indian industry. It also examines abnormal share returns throughout a period surrounding the announcement of both successful and unsuccessful acquisition and merger bids. The overall results indicate that related construction mergers create wealth for shareholders of the target firms.

KEYWORDS

acquisitions & mergers, chemical industry, shareholder value analysis.

INTRODUCTION

Mergers and acquisitions are increasingly becoming strategic choice for organizational growth and achievement of business goals including profit, empire building, market dominance and long term survival. The ultimate goal of this strategic choice of inorganic growth is, however, maximization of shareholder value. The phenomenon of rising M&A activity is observed world over across various continents, although, it has commenced much earlier in developed countries (as early as 1895 in US and 1920s in Europe), and is relatively recent in developing countries. In India, the real impetus for growth in M&A activity had been the ushering of economic reforms introduced in the year 1991, following the financial crisis and subsequent implementation of structural adjustment programme under the aegis of International Monetary Fund (IMF). In recent times, though the pace of M&As has increased significantly in India too and varied forms of this inorganic growth strategy are visible across various economic sectors.

The term mergers and acquisitions encompass varied activities of stake acquisition and control of assets of different firms. Besides, there are several motives for different types of mergers and acquisitions seen in corporate world.

REVIEW OF LITERATURE

Dodd (1980) finds that shareholders of target firms earn large positive abnormal returns from announcement of merger proposals. These announcement period returns range from 13% at the announcement date of the offer to 33.96% average over the duration of the merger proposal i.e. 10 days before and 10 days after the announcement. On the other hand, shareholders of bidder firms experience negative abnormal returns of 7.22% and 5.50% over the duration of the proposals.

Malatesta (1983) examined a matched sample of targets and their bidders in 30 successful mergers and finds a significant average increase of $32.4 million (t = 2.07) in their combined equity value in the month before and month of outcome announcement. The acquired (target) firms gained more than the acquirer forms. The target firms earned $18.6 million (t = 5.41) of the combined increase in the equity value while acquiring firms earned $13.8 million (t = 0.91).

PROBLEM OF THE STUDY

Through the strategy of M&A thus, the acquiring firm intends to improve its long term operating and financial performance. The major focus is on improving long term profitability of firms, improve the efficiency of utilization of existing and acquired assets and make the acquirer firm more stable in the long run to address competitive forces and command sizeable market share.

RESEARCH METHODOLOGY

Research is an art of scientific investigation. According to Redman & Mory defines research as a "Systematic effort to gain Knowledge".

RESEARCH DESIGN

According to Kerlinger, "Research Design is the plan structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance." The research design undertaken for the study is analytical one. A researcher use facts or information already available and analyze those to make critical evaluation of the material. It is quantitative in nature.

DATA COLLECTION

SECONDARY DATA

Company Profile, annual reports, Websites, Magazines, articles are used widely as a support to secondary data. Print media and internet has been used for data collection.

PERIOD OF STUDY

The study covers M&A in India during the period from financial year 2005- 2016 through 2005-2006. The study period is divided as pre-merger and post merger period for each case of M&A depending upon the year of merger for each M&A deal. Pre-merger as well as post-merger period comprises of 3 years each. The year in which merger/acquisition has taken place is excluded from the study so as to allow for post-merger adjustments and integration issues.

SAMPLE DESIGN

The study basically follows judgemental sampling. The sample for the study primarily includes mergers by public limited companies listed on BSE, during the period of study. Only domestic mergers are included in the study.

OBJECTIVES OF THE STUDY

1. To examine the trends in M&A in India
2. To examine pre-merger and post-merger operating and financial performance of firms in M&A deals

ANALYSIS AND INTERPRETATION

MERGERS AND ACQUISITIONS IN INDIA

TABLE 1

Year Aggregate	M&A	Mergers	Acquisitions
2005-06	33	NA	NA
2006-07	124	NA	NA
2007-08	248	NA	NA
2008-09	387	NA	NA
2009-10	1469	288	1181
2010-11	1340	287	1053
2011-12	1169	323	846
2012-13	1047	216	831
2013-14	1041	252	789
2014-15	1243	373	870
2015-16	1261	347	914

Source: CMIE M&A, CMIE Business Beacon Database and Kar, R. (2016)

NA: Not Available

The following important observations can be, made from above table:

(i) A total of 9,631 M&A transactions have occurred during the entire period from 2005-06 to 2015-16. The maximum number of M&A transactions is reported during the year 2010-11 (1,469) while the lowest are observed during the year 2005-06 (33).

(ii) The number of M&A deals has grown at CAGR (Compounded Annual Growth Rate) of 35.47% during study period.

(iii) The number of M&As during early periods of economic reforms are found to be negligible in comparison to those observed during the later part of study period. There were only 33 M&As during the year 2005-06 and this figure rose to 387 during the year 1999-2000. Further, within this period, a considerable decline is observed in year-on-year increase in M&As. From 33 M&As in 2005-06, the number rose by a significant 124 which is 275.76% increase from the figures of 2005-06. In the following year however, the total M&A deals increased to 248 accounting for a comparatively low 100% growth on year-on-year basis.

(iv) The year 2008-09 recorded the worst increase during this period of only 21 M&A deals in comparison to previous year figures that accounted for a negligible 8.47% increase. The percentage increase in M&A deals improved during the year 2009-2010 to 43.87% with 387 transactions reported during this year. The total number of M&As reported during this period of five years is 1,061 which accounts for a mere 11.02% of the total (9,631) M&As recorded during the entire period of study.

PERCENTAGE CUMULATIVE ABNORMAL RETURNS OF SAMPLE ACQUIRER FIRMS IN MANUFACTURING SECTOR IN INDIA

TABLE 2

Acquirer	Pre-Announcement period			Post- Announcement period			Around Announcement period		
	(t-20)	(t-10)	(t-5)	(t+5)	(t+10)	(t+20)	(t-20, t+20)	(t- 10, t+10)	(t-5, t+5)
Chemical Sector									
Bayer India Ltd	35.42	29.57	19.49	-6.5	0.76	-1.12	29.64	25.67	8.33
Futura Polyesters	25.2	-20.07	-10.07	9.12	1.84	.68.20	100.06	7.21	5.7
Kissan Mouldings Ltd	25.45	16.29	16.86	6.47	18.08	31.15	50.63	28.5	17.36
Berger Paints	-47	-52.28	4.19	1.19	0.7	-5.32	-50.6	-49.86	7.1
Beck India	-36.6	-27.01	-20.19	0.52	2.45	-4.39	-40.74	-24.3	-19.41
Sree Rayalaseema Hi - Strength Hypo Ltd	-15.27	-5.25	-4.83	20.78	33.15	12.41	-2.25	28.51	16.56
Castro! India	7.58	2.66	1.51	5.85	8.4	-4.52	-1.73	6.26	2.57
Dharamsi Morarji chemicals Ltd	-2	-1.33	-2.11	1.91	-5.67	-6.03	-8.04	-7.01	-0.21
BASF	-17	-8.35	-5.72	10.26	6.44	-1.92	-18.83	-1.82	4.63
Arvind International	-50.43	-10.09	17.18	-40.61	-3.07	-45.62	-54.82	-8.59	-18.86
Exide Industries	7.12	3.53	5.21	5.95	23.43	13.71	19.82	25.95	10.15
Average CAR	**-6.14**	**-6.58**	**1.96**	**1.36**	**7.86**	**5.14**	**2.1**	**2.77**	**3.08**
t Statistics	**-0.684**	**-1.001**	**0.524**	**0.29**	**2.16 ****	**0.608**	**0.151**	**0.371**	**0.839**

The analysis of announcement period returns for acquirers in chemicals sector indicate that Average CARs are substantially lower during pre-announcement period for acquirers while the same increases during post-announcement period. Average CAR for acquirers in Chemical Sector are -6.14% during (t-20) window which is however, not statistically significant. On the other hand average CAR is 5.14% during (t+20) window which again though is not statistically different from zero. However, average CAR for period of 10 days after announcement (7.86%) is found to be statistically significant at 5% level. statistical significance could not be established for average CARs for acquires in chemical sector, the indication of high number of positive CAR in all the observations for the sector provides a weak evidence of positive short term gains to shareholders in this sector.

SUMMARY OF FINDINGS

- The pre-liberalization era severely restricted mergers and acquisitions in India by imposing regulatory restrictions through multiple legislations like FERA, MRTP and licensing system. In particular, there was lot of discouragement to horizontal combinations. The real impetus was given to mergers and acquisitions through the 1991 economic reforms that encouraged liberalization, privatization and globalization. Easing of regulations, sale of state-owned companies, overcapacity and deregulation of fragmented industries gave boost to M&A in India.
- A total of 9,631 M&A transactions have occurred during the entire period from 1995-96 to 2006-07. The number of M&A deals has grown at CAGR (Compounded Annual Growth Rate) of 35.47% during study period.
- Sectoral analysis of announcement period returns indicate that Average CARs are substantially lower during pre-announcement period for acquirers in Chemical Sector while the same increases during post-announcement period. Average CAR for acquirers in Chemical Sector are -6.14% during (t-20) window but 5.14% during (t+20) window. However, average CAR for period of 10 days after announcement (7.86%) only is found to be statistically significant for acquirers in chemical sector.

SUGGESTIONS

- Since mergers and acquisitions have not found to be contributing - significantly to profitability, liquidity and solvency or operational efficiency, the acquirers need to assess whether paying substantial purchase considerations for these transactions is economically viable for the firm in the long run. Given the fact that acquisitions premiums are rising, it becomes imperative for acquirers to evaluate the inorganic growth strategy against the organic growth options available.
- The acquirers need to identify appropriate target that has complimentary fit within the acquirers own organizational structure, product portfolio and work culture. Post merger integration issues may be one significant reason for failure of M&As to improve long term operating and financial performance of acquirer companies. As Machi (2005) suggests, organization structure with similar management problems, cultural system and structure will facilitate the effectiveness of communication pattern and improve the company's capabilities to transfer knowledge and skills.

SCOPE FOR FURTHER RESEARCH

- The study can be extended to more sectors based on availability of data in future.
- Future research on the topic can also be directed to include cross border mergers and acquisitions which are increasingly becoming significant in Indian economy.
- A detailed sectoral analysis of these mergers and acquisitions can be made to identify if there are any concrete gains to acquirers. This is particularly important given that cross border M&As involve a very large purchase consideration.

CONCLUSION

Regulatory changes and economic reforms have been major reasons for bringing significant changes in M&A scene in India. The major reasons for increasing consolidations in India are the industry specific advantages, cost reduction, exploiting core competence and global competition. These factors have skewed the M&A activity in India towards horizontal and vertical mergers and acquisitions. The diversified M&A have been thus reduced to negligible number.

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