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NEED/IMPORTANCE OF THE STUDY

STATEMENT OF THE PROBLEM

OBJECTIVES

HYPOTHESES

RESEARCH METHODOLOGY

RESULTS & DISCUSSION

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RECOMMENDATIONS/SUGGESTIONS

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SCOPE FOR FURTHER RESEARCH

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APPENDIX/ANNEXURE

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- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

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- Always indicate the date that the source was accessed, as online resources are frequently updated or removed.

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MERGERS AND ACQUISITIONS IN INDIAN INFORMATION TECHNOLOGY INDUSTRY AND ITS IMPACT ON SHAREHOLDERS' WEALTH

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ABSTRACT

Numerous academic studies are available on merger announcements and their impact on market valuation of equity or shareholders' wealth, but there is hardly any documented evidence for Indian Information Technology Industry. In this research on "Mergers and Acquisitions in Indian Information Technology Industry and its Impact on Shareholders' Wealth", an attempt is made to know the wealth effects of mergers and acquisitions in the Indian Information Technology Industry during the period 2008-2010. For this, an event study analysis has been conducted from the point of view of shareholders of the acquiring companies to ascertain whether shareholders' of acquiring companies have been benefited or not.The analysis reveals that the shareholders of the acquiring firms did not gain significant abnormal returns and the mergers and acquisitions did not have any impact on the shareholders' wealth. The analysis of the individual deals also reveals that no deal has benefited their respective shareholders.

KEYWORDS

Information Technology Mergers, Market Valuation of Mergers, Event Study Analysis.

INTRODUCTION

The business environment today has become more dynamic and firms need to cope with this dynamic environment to grow. The growth for firms can be organic or inorganic. Most of the firms in their quest for growth choose the route of inorganic growth. Mergers and acquisitions being one such route is been prominently used by business firms in the last decade or so. We can see mergers and acquisitions happening throughout the world. In the United States, the first merger wave occurred between 1890 and 1904 and the second began at the end of the World War I and continued through the 1920s. The third merger wave commenced in the latter part of World War II and continues to the present day. About two-thirds of the large public corporations in the USA have merger or amalgamation in their history.

In India, Mergers and acquisitions have been more in number and value in the last decade or so. The total number of mergers and acquisitions in 1999-2000 was 1068 and the value of acquisitions was Rs.32,012 crores. In 2000-01 the total number was 1215 and value of acquisitions being Rs.29,218 crores. In 2006-07 the number increased to 1418 and the value of acquisitions to Rs.2,38,191 crores. In 2009-10 the number of deals were 823 and the value of acquisitions was Rs.1,39,921 crores and in 2010-11 till February the number of deals were 733 and the value of acquisitions amounted to Rs. 1,78,154 crores. Thus Mergers and Acquisitions, the way in which they are understood in the Western countries, have started taking place in India in the last decade. Now with lot of mergers and acquisitions happening in Indian context it is essential to understand whether such a strategic decision taken by the firm has led to any increase in the performance of the company. The merger or an acquisition is justified only when it has yielded the desired results to the stakeholders. The decision taken by firms should result in creation of wealth to the shareholders. There has been research done to know whether strategic decisions like merger or an acquisition have any effect on the shareholders wealth. The effect of an event like M&A can be viewed from two perspectives: An Accounting perspective and Market perspective. The studies done, both in India and abroad have taken into consideration the market approach. A brief review of literature is been done to get an understanding of the research done to know the effect of an event like merger on the shareholders wealth.

REVIEW OF LITERATURE

This section provides some important research on the effect of merger and acquisitions on the shareholders wealth. Studies so far include both domestic and cross border merger and acquisitions and also are based on overall data and on different sectors. Andrade et al (2001) in their paper mentioned that on average acquirers destroy shareholders value or they do not create value. The studies do not find any support for the value creation for the shareholders at the time of acquisition. On the other hand the market reaction to the target firms is positive and significant at the time of acquisition announcement. Combined wealth effect of acquirers and targets are also positive.

Jensen and Ruback (1983) and Jarrell et al (1988) conclude that the mergers seem to create value but the value is accrued entirely to target firms and the acquirers either destroy value or they do not create any value. Some recent studies (Shleifer and Vishny, 2003; Rhodes-Kropf & Viswanathan, 2004; Dong et al, 2006) followed the market valuation approach to answer some of the empirical findings in merger and acquisition. They argue that mergers are driven by the valuation in the market. Some studies are country specific, mainly between developed and developing countries. Recent studies have made attempt to understand the wealth effect of acquisitions made by developing country firms of developed country firms. International acquisitions by Indian firms have been examined by Zhu and Malhotra (2008) and Gubbi et al (2009). Zhu and Malhotra (2008) empirically examined the announcement effect of cross-border acquisitions by Indian firms for the period of 1999 to 2005. Their study shows that the Indian stock market reacts positively to the acquisition announcement. However, positive abnormal return last for three days, after that it becomes negative. Gubbi et al (2009) did an event study of 425 cross-border acquisitions by Indian firms during 2000-2007. They also showed that the Indian acquirers created value in international acquisitions and the value created is higher when the target firms are located in advanced economic and institutional environments. Manoj Anand and Jagandeep Singh (2008) in their study on bank mergers in India found significant return to both bidder firm and target firm shareholders. Aigbe Akhibge and Anna D. Martin (2002) in their study on Microsoft found that Microsoft's acquisitions in the internet/online services segment adversely affected the stock prices of internet/online services rival portfolio. The results of the study do not indicate that the financial market perceives Microsoft's operating-system acquisitions instrumental in achieving synergies from Microsoft's dominant role in the operating system segment to the detriment of its internet/online services rivals. The study found rivals to respond favourably to Microsoft's operating system acquisitions. This study is more company specific when compared to studies in other sectors. Kohers, Ninon, Kohers, Theodor (2000): in their study found that the distinctive high-growth, high-risk nature of technology-based industries raises important questions about the creation of wealth in high-tech takeovers. The results show that acquirers of high-tech targets experience significantly positive abnormal returns, regardless of whether the merger is financed with cash or stock. Factors influencing bidder returns are the time period in which the merger occurs, the ownership structure of the acquirer, the high-tech affiliation of acquirers, and the ownership status of the target.

Thus it is evident that while studies are be done mainly on overall basis both involving domestic as well as cross border mergers and acquisitions but sector specific studies are very few and in case of India studies are mainly done on banking sector. Here an attempt is been made to understand the effect of a merger or an acquisition on the wealth of the shareholders with reference to Information Technology.

NEED FOR THE STUDY

Mergers and Acquisitions, being part of growth strategy, have been adopted by most of the companies in India. There are certain sectors where we find lot of activities and more so in service sectors. We find that studies are been done in Banking sector in India. However we do also find lot of M&A activities in other sectors too. Hence to know the performance of these events it is essential to study their impact on shareholders' wealth. The present study is related to Indian Information Technology Industry. Further studies can also be done on different sectors involved in both domestic and cross-border mergers and acquisitions.

OBJECTIVES OF THE STUDY

The objectives of this study are as follows:

1. To know the effect of cross-border mergers and acquisitions on the wealth of shareholders of the acquitting companies in Indian Information Technology Industry.
2. To know the effect of domestic mergers and acquisitions on the wealth of shareholders of the acquitting companies in Indian Information Technology Industry.

Based on the above objectives the following hypothesis are developed

HYPOTHESIS 1

H_0: Cross Border Mergers and Acquisitions do not have impact on the shareholders' wealth of acquiring companies.
H_1: Cross Border Mergers and Acquisitions do have impact on the shareholders' wealth of acquiring companies.

HYPOTHESIS 2

H_0: Domestic Mergers and Acquisitions do not have impact on the shareholders' wealth of acquiring companies.
H_1: Domestic Mergers and Acquisitions do have impact on the shareholders' wealth of acquiring companies.

RESEARCH METHODOLOGY

In conducting this study the data are obtained from CMIE Prowess database. Daily adjusted closing prices of stocks and the market index (BSE 500) are obtained from BSE website. The Acquirer and Target Company are public limited companies and are listed on the stock exchange. A total of 18 companies were obtained who have undertaken domestic and cross border mergers or acquisitions during the period from January 2008 to August 2010. Out of these 10 companies have made a total 12 cross border mergers and acquisitions and 10 companies were involved in domestic merger or acquisition. Glodyne Technoserve Ltd and Wipro Ltd have undertaken both domestic and international mergers. The study is based on the performance of acquiring and target companies in the observations. The event study methodology used in our analysis is quite straight forward and conventional (MacKinlay, 1997). An even study is an econometric method to measure the impact on a company from a certain event and is one of the most used empirical methods in finance and accounting. The event study methodology was introduced by Fama et.al. in the paper "The adjustment of stock prices to new information" of measuring changes in security prices from an event or announcement. An event study is an econometric method to measure the impact on a company from a certain event and is one of the most used emphirical methods in fiancé and accounting. Accordingly to the efficient market hypothesis the effects of an event will immediately be reflected in the security prices and the event study methodology has its strength in measuring these implications

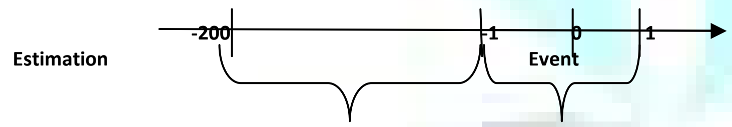
THE EVENT WINDOW

The event window determines the number of days over which we measure the possible abnormal return caused by the event. The theory of the efficient market hypothesis proposes that any shift in stock prices caused by the event will happen immediately due to rational behaviour which talks in favour of short event window since a long window could risk diluting the possibility if finding any significant evidence. However if the event window is too short we risk not catching the effect of the event if the information comes out after the closing of market and therefore doesn't reaches the public until the next day or if the information is leaked the day before the announcement and therefore causes the effect the day before the actual announcement/event day.

THE ESTIMATION PERIOD

The estimation period is used to estimate the expected return of the stocks. The period therefore needs to be long enough to create a respective measure of returns but too long and estimation period can risk biasing the estimation with information from other events or changes in the firms general conditions. It is normally set at around a year of prior to the event window. In this paper it is set to 200 days when the weekends are excluded.

TIMELINE –



To ensure that any information leakage is being captured, the identified merger period includes 20 days before and 20 days after the event (-20 to +20). The reason for considering such a window is that our objective is to evaluate the impact of the merger on shareholders' wealth of the acquiring and target companies around the day of the official announcement. The event window of (-15 to +15), (-10 to +10) and (-5 to +5)) have also been analysed to evaluate the impact as the deal got closer and also to study the impact in short run periods. The analysis is based on secondary data. For the sample selected for the study Cumulative Abnormal Returns (CAR) are calculated using a standard event study analysis. Abnormal returns, that indicate the additional impact on stock returns due to an event over and above normal market movements, are computed as follows:

$$AR_{i\tau} = R_{i\tau} - \hat{\alpha}_i - \hat{\beta}_i R_{m\tau}.$$

Where, Rit is the daily return on firm 'i' on day't' and Rmt is the return on the bench mark index, α and β are OLS regression parameters that are estimated using the market model over the previous period of 200 days (Estimation Window).

AGGREGATION OF ABNORMAL RETURNS

The abnormal return observations must be aggregated in order to draw overall inferences for the event of interest. The aggregation is along two dimensions – through time and across securities. We will first consider aggregation through time for an individual security and then will consider aggregation both across securities and through time. The concept of cumulative abnormal return is necessary to accommodate a multiple period event window. Define $CAR_t(T_1,T_2)$ as the sample cumulative abnormal return (CAR) from T_1 to T_2 where $\mathbf{T_1 < T_1 \leq T_2 \leq T_2}$. The CAR from T_1 to T_2 is the sum of the included abnormal returns,

$$\mathbf{CAR_t(T_1, T_2) = \sum_{T=T_1}^{T_2} AR_{iT}}$$

The average of CAR will help you receive to the CAAR (Cumulative Average Abnormal Return)

The cumulative abnormal returns are computed for acquiring companies and target companies and the significance of Cumulative average abnormal returns is tested by calculating the t statistic value.

RESULTS AND DISCUSSIONS

The earlier studies on impact of mergers and acquisitions on shareholders wealth shows that the acquiring company shareholders don not gain any significant abnormal returns in and around the announcement date. The results of this study are consistent to the earlier studies which conclude that the shareholders of the acquiring company will have a negative abnormal return around the announcement date.

TABLE 1: CUMULATIVE ABNORMAL RETURNS OF SAMPLE COMPANIES INVOLVED IN CROSS BORDER MERGERS AND ACQUISITIONS FOR WINDOW PERIODS -20+20, -15+15, -10+10 AND -5+5 DAYS

Acquirer Company	Target Company	CAR -20+20	CAR -15+15	CAR -10+10	CAR -5+5
Glodyne Technoserve Ltd	Decision one Inc USA	-19.13	-20.09	-10.76	-3.42
GSS America Infotech Ltd	ATEC Group USA	-8.85	-23.47	-13.72	-5.78
HCL Technologies Ltd	Capital Stream Inc-USA	-3.82	-0.33	16.38	-0.29
HCL Technologies Ltd	NTS Group UAE	42.98	24.49	12.97	12.46
Helios & Matheson Information Technology Ltd	Helios & Matheson North America Inc. USA	-1.18	-8.75	-18.66	-4.40
Mascon Global Ltd	Ebusinessware Inc USA	-17.00	0.02	8.59	-5.71
Mindteck (India) Ltd	Prime Tech Solutions USA	-14.16	-18.95	-16.65	2.16
Prithivi Information solutions Ltd	Precentix Inc USA	-29.00	-32.07	-27.88	-13.08
Rolta India Ltd	OneGIS Inc USA	-10.58	-3.80	-3.67	0.88
Rolta India Ltd	Whittman Hart USA	22.62	10.44	-7.00	6.83
Sileverline Technologies Ltd	OMDR Inc Canada	-37.87	-22.48	-23.33	-6.76
Wipro Ltd	Nokia Mobile Broadcast solutions Finland	8.42	11.00	13.17	23.41

Table 1 provides Cumulative abnormal returns for sample companies for event windows of -20+20,-15+15, -10+10 and -5+5. The cumulative abnormal return for the event window -20+20 of the sample companies shows a mixed result. While HCL Technologies acquiring NTS group of UAE earned an abnormal return of 43% to its shareholders but shareholders of Silverline Technologies suffered substantial loss to the extent of 38%. In the event window of -15+15, shareholders of Prithivi Information Solutions Ltd are major losers(-32%) but shareholders of HCL Technologies earned an abnormal return of 24.5%. Similarly for the event window of -10+10 HCL Technology shareholders have gained while again shareholders of Prithivi Information have lost value. In a shorter window of -5+5 the shareholders of Wipro Ltd have gained substantially i.e 23.41%.

Thus from the above table we can see a mixed reaction from the stock market around the announcement of an international merger or an acquisition by an information technology company. Better known companies have gained substantially, as the acquisition by such companies are viewed positively by the market. However shareholders of lesser known companies tend to lose on an international merger or an acquisition as the market reacts negatively to such an announcement. The possible reason for mixed behaviour of the market needs to be studied further but one possible reason could be the maturity of the Indian stock market.

TABLE 2: CAAR AND T STATISTIC FOR EVENT WINDOWS -20+20,-15+15, -10+10 AND -5+5

Event Window	CAAR	t statistic
-20+20	-5.63	-0.88
-15+15	-7.85	-1.67*
-10+10	-7.25	-1.77*
-5+5	-1.12	-0.56

***, **, *** indicates statistical significance at 10%, 5% and 1% respectively**

The Cumulative Average Abnormal Returns of the sample for different event window along with t statistic value have been provided in table 2. The overall sample gives a negative CAAR for different event windows. The -20+20 window gives a negative CAAR which is statistically insignificant. Similar negative return for -15+15, -10 +10 can be seen which is statistically significant and -5+5 can be seen with t statistic value which is statistically insignificant.

Table 3 provides information of the Cumulative abnormal returns of sample observations for different event windows. The result shows that the acquirer company has failed to create any significant wealth to shareholders'. All the firms in the study have shown negative CAR except for Allied Digital Communications which showed positive CAR for all the windows.

TABLE 3: CUMULATIVE ABNORMAL RETURNS OF SAMPLE COMPANIES INVOLVED IN DOMESTIC MERGERS AND ACQUISITIONS FOR WINDOW PERIODS -20+20, -15+15, -10+10 AND -5+5 DAYS

Acquirer Company	Target Company	CAR (-20 to +20)	CAR (-15 to +15)	CAR (-10 to +10)	CAR (-5 to +5)
3i Infotech Ltd.	3i Infotech B P O Ltd.	-1.379	-1.207	-1.743	-3.777
3i Infotech Ltd.	E-enable Technologies Pvt. Ltd.	-0.24	-0.296	0.262	0.323
3i Infotech Ltd.	J & B Software (India) Pvt. Ltd.[1]	1.077	1.524	1.926	1.407
3i Infotech Ltd.	Stex Software Pvt. Ltd.	-0.535	-0.026	0.087	0.807
3i Infotech Ltd.	A O K In-house B P O Services Ltd.[2]	-0.24	-0.296	0.262	0.323
Allied Digital Services Ltd.	En Pointe Technologies India Pvt. Ltd.	1.385	1.562	2.938	3.441
Aptech Ltd.	Aptech Software Ltd.	-0.17	-0.32	-0.8	-0.625
Glodyne Technoserve Ltd.	Compulink Systems Ltd. [merged]	-0.601	-0.602	-0.117	-0.9
K P I T Cummins Infosystems Ltd.	K P I T Cummins Global Business Solutions Ltd.	-0.352	-1.091	-1.241	-1.408
Mindtree Ltd.	Aztecsoft Ltd. [merged]	0.172	0.305	-0.283	-0.614
Mindtree Ltd.	Mindtree Wireless Pvt. Ltd. [merged]	-1.064	-1.126	-1.208	-1.767
Polaris Software Lab Ltd.	Laser Soft Infosystems Ltd.	-0.006	0.173	0.426	0.58
Tata Consultancy Services Ltd.	T C S E-serve Ltd.	-0.393	-0.244	0.587	-0.021
Tech Mahindra Ltd.	I-policy Networks Ltd. [merged]	0.196	-0.039	-0.099	-0.313
Tech Mahindra Ltd.	Satyam Computer Services Ltd.	-0.32	-0.768	-0.631	-0.822
Wipro Ltd.	Wipro Technology Services Ltd.	-0.22	-0.267	-0.186	-0.192

[1]3i Infotech Ltd has also announced the merger with Fineng Solutions Pvt. Ltd and Taxsmile.com India Pvt. Ltd on the same day

[2]3i Infotech Ltd has also announced the merger with Elegon Infotech Ltd on the same day

All the observations across event windows have not yielded significant abnormal returns to the shareholders Allied Digital has performed better than all other observations across all the event windows. The analysis of the abnormal returns of individual company security across different event windows reveals that they have given negative cumulative abnormal returns to the shareholders in most of the cases. For event window -20 to +20, all the observations have negative

cumulative abnormal returns except for Allied Digital Services Ltd. and for one case of 3i Infotech Ltd. and for event window (-15 to +15), the shareholders of Allied Digital Services Ltd and for one observation of 3i Infotech Ltd. have gained more average abnormal returns than any other observation in the event window. Similarly for event window -10 to +10 and -5 to +5 most of the observations show a negative abnormal returns except for those two cases reported above which have given abnormal returns to their shareholders. However it is worth to note that for one observation of 3i Infotech Ltd the result shows negative abnormal returns for all event windows. Thus, the event of the individual observations has had negative impact on the wealth of their respective shareholders.
Table 4 reports the Cumulative Average Abnormal Returns (CAAR) across companies for different event windows along with their t statistic value.

TABLE 4: CAAR ACROSS COMPANIES FOR EVENT WINDOWS -20+20,-15+15, -10+10 AND -5+5 WITH T STATISTIC VALUE

Event Window	CAAR	t statistic
-20+20	-0.77	0.242
-15+15	0.03	0.009
-10+10	4.29	0.808
-5+5	-0.42	-0.064

***, **, *** indicates statistical significance at 10%, 5% and 1% respectively**

The CAAR for event window -20+20 across sample companies involved in domestic mergers and acquisitions shows a statistically insignificant negative CAAR. Similar results can be seen for event windows -15+15 and -5+5. However CAAR for event window -10+10 shows significant positive returns to the shareholders. The above results reveal that the stock market reacts negatively to a merger announcement made by the company and shareholders tend to lose significant wealth in and around the announcement date. These results are consistent for both individual and across sample companies for all event windows except for -10+10 which shows significant positive returns.

FINDINGS

The results of the study provides evidence than in case of cross-border mergers and acquisitions most companies have shown a negative CAR, thus suggesting shareholders value destruction in and around the announcement date. The wealth destruction is evident for both individual securities and cross-sectional analysis. Most of the earlier studies also show similar results. Most of the Indian acquiring company shareholders tend to lose their wealth in short run on the announcement of either cross border or domestic merger or an acquisition by an Indian IT company. However as a precaution this cannot be generalised due to the fact that Indian companies are still in the nascent stage of cross border mergers and acquisitions. Lack of experience of the Indian companies to International acquisitions and a less matured stock market may be major reasons for such negative reactions. This study can be further extended to different sectors to know the effect of such events on shareholders wealth. Further studies can be to understand the determinants of cross border mergers and acquisitions.

CONCLUSION

This research paper is an attempt to provide an analysis of Cross Border and domestic Mergers and Acquisitions in Indian Information Technology Industry from the perspective of acquiring company shareholders. The analysis shows that the mergers and acquisitions did not have positive impact on the shareholders' wealth. The event study analysis results show that acquiring companies' market value of equity has been reduced on the immediate announcement of mergers. It can be concluded that the mergers and acquisitions in the study did not have an impact on the shareholders' wealth across securities as well as for individual securities.

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