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CONTENTS

Sr. No.	TITLE & NAME OF THE AUTHOR (S)	Page No.
1.	DO EXECUTIVE DIRECTORS MANIPULATE EARNINGS? SEYED HOSSEIN HOSSEINI & MOHAMADREZA ABDOLI	1
2.	MANAGEMENT EDUCATION – IMPACT OF VALUE ORIENTATIONS ON CAREER & BUSINESS PUSHPA SHETTY	7
3.	STRATEGIC GAINS OF BY-PRODUCT MARKETING: A STUDY ON SELECTED COMPANIES OF BANGLADESH GOLAM MOHAMMAD FORKAN & TAHSAN RAHMAN KHAN	13
4.	THE EFFECT OF CURRENCY DEVALUATION ON THE ETHIOPIAN ECONOMY'S TRADE BALANCE: A TIME SERIOUS ANALYSIS FIKREYESUS TEMESGEN & MENASBO GEBRU	17
5.	MUTUAL FUNDS IN INDIA: AN ANALYSIS OF INVESTORS PERCEPTIONS DR. PRASHANTA ATHMA & K. RAJ KUMAR	21
6.	FINANCES OF CENTRE FOR DISTANCE EDUCATION, OSMANIA UNIVERSITY, HYDERABAD, ANDHRA PRADESH: AN ANALYTICAL STUDY G. VENKATACHALAM & P. MOHAN REDDY	27
7.	THE INFLUENCE OF MARKETING ON CONSUMER ATTITUDE FUNCTIONS FOR KITCHENWARE, A STUDY WITH SPECIAL REFERENCE TO KOCHI METRO ANILKUMAR. N	32
8.	BEHAVIOURAL FINANCE: A NEW PERSPECTIVE FOR INVESTMENT IN FINANCIAL MARKET DR. SREEKANTH. M S	39
9.	THE EFFECT OF MERGER AND ACQUISITIONS ON THE SHAREHOLDERS' WEALTH: EVIDENCE FROM THE FOOD INDUSTRY IN INDIA DR. RAMACHANDRAN AZHAGIAH & T. SATHISH KUMAR	42
10.	WHETHER DIFFERENCES MAKE DIFFERENCES? A NEW PARADIGM ON WORKFORCE DIVERSITY D. RAMADEVI & DR. S. A. SENTHIL KUMAR	54
11.	CORPORATE SOCIAL ENGAGEMENT: NEW BASE LINE TO CORPORATE SOCIAL RESPONSIBILITY KAVITA MEENA	59
12.	GREEN MARKETING BRIJESH SIVATHANU PILLAI & KANCHAN PRANAY PATIL	64
13.	MARKET EFFICIENCY AND INTERNATIONAL BENCHMARKS IN THE SECURITIES MARKET OF INDIA – A STUDY DR. MUNIVENKATAPPA	74
14.	CHALLENGE OF LIQUIDITY RISK AND CREDIT RISK IN INSURANCE COMPANIES WITH SPECIAL REFERENCE TO INDIAN PUBLIC SECTOR GENERAL INSURANCE COMPANIES AVINASH TRIPATHI	82
15.	CONTEMPORARY ISSUE ON DEREGULATION OF SAVING ACCOUNT INTEREST RATE DR. RAJIV GANDHI	87
16.	A STUDY ON THE EFFECT OF FOOD ADVERTISEMENTS ON CHILDREN AND THEIR INFLUENCE ON PARENTS BUYING DECISION GINU GEORGE	92
17.	DETERMINANTS OF CORPORATE DIVIDEND POLICY IN SELECT PRIVATE SECTOR CEMENT COMPANIES IN TAMIL NADU - AN EMPIRICAL ANALYSIS DR. V. MOHANRAJ & DR. N.DEEPA	107
18.	THE ROLE OF 'FOLLOW THE NEIGHBOUR' STRATEGY AND FACTORS INFLUENCING INVESTMENT DECISION WITH REFERENCE TO NASIK CITY BHUSHAN PARDESHI, PAVAN C. PATIL & PADMA LOCHAN BISOI	110
19.	IMPACT OF ADVERTISING ON BRAND RECALL AND BRAND PERSONALITY FORMATION: A STUDY OF ORGANISED FASHION RETAILING HIMANSHU SHEKHAWAT & PREETI TAK	116
20.	A CASE STUDY ON STRESS MANAGEMENT IN WORKING WOMEN IN GOVERNMENT\SEMI-GOVERNMENT ENTERPRISES IN SHIMLA, (H.P.) SHALLU SEHGAL	122
21.	LEVERAGE ANALYSIS AND ITS IMPACT ON SHARE PRICE AND EARNING OF THE SELECTED STEEL COMPANIES OF INDIA – AN EMPIRICAL STUDY MUKESH CAJMER	129
22.	A STUDY ON LEVEL OF EXPECTATION OF MUTUAL FUND INVESTORS & IMPACT OF DEMOGRAPHIC PROFILE ON PERIOD OF INVESTMENT IN MUTUAL FUND TARAK PAUL	136
23.	IMPACT OF MERGERS & ACQUISITIONS ON FINANCIAL PERFORMANCE: WITH SPECIAL REFERENCE TO TATA GROUP NEHA VERMA & DR. RAHUL SHARMA	140
24.	EXPLORING SERVICE INNOVATION PROCESS AND STRATEGY IN DEVELOPING CUSTOMER RELATIONSHIP-WITH REFERENCE 21st CENTURYBANK 'YES BANK' SHILPA SANTOSH CHADICAL & DEBLINA SAHA VASHISHTA	144
25.	EMPLOYEE LOYALTY ABOVE CUSTOMER LOYALTY AFREEN NISHAT A. NASABI	152
26.	FDI IN MULTIBRAND RETAILING IN INDIA: PERCEPTION OF THE UNORGANISED RETAILERS IN BUSINESS CAPITAL OF UTTARAKHAND DEEPAK JOSHI	156
27.	COMPARATIVE STUDY OF SELECTED PRIVATE SECTOR BANKS IN INDIA NISHIT V. DAVDA	161
28.	IMPACT OF HRM PRACTICES ON PERFORMANCE OF NON-ACADEMIC EMPLOYEES OF OPEN UNIVERSITIES IN INDIA B. LAXMINARAYANA	167
29.	POST-MERGER FINANCIAL PERFORMANCE APPRAISAL OF ACQUIRING BANKS IN INDIA: A CASE ANALYSIS AZEEM AHMAD KHAN	172
30.	MANPOWER REQUIREMENT ASSESSMENT CONSIDERING THE MAKE OR BUY DECISION POLICY OF CENTRAL WORKSHOP IN AN INTEGRATED STEEL & POWER COMPANY AKHILESH JHA, SOUPOARNO MUKHERJEE & RANDHIR KUMAR	176
	REQUEST FOR FEEDBACK	181

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RESULTS & DISCUSSION

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IMPACT OF MERGERS & ACQUISITIONS ON FINANCIAL PERFORMANCE: WITH SPECIAL REFERENCE TO TATA GROUP

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ABSTRACT

The process of mergers and acquisitions (M&A) has gained significant importance in today's corporate world. This process is extensively used for increasing revenues and profitability, restructuring the business organizations, increased market share and to eliminate competition. The concept of merger and acquisition in India became popular in the year 1988. This study aims to study the impact of mergers and acquisitions on the financial performance of Tata Group, by examining some pre and post-M&A financial ratios, with the sample of companies chosen between 2003-04 and 2007-08. The results from the present study of the pre and post M&A financial performance ratios of the Tata Group reveals that there was no significant increase/decrease in the financial ratios i.e. the M&A's has not significantly affected the financial performance of Tata Group.

KEYWORDS

Financial performance, Mergers and Acquisitions (M&A), Pre and post financial ratios.

INTRODUCTION

Waves of mergers and acquisitions (M&A) have been a characteristic of corporate history. The current trend towards international mergers, acquisitions, strategic alliances and joint ventures is resulting in organizations having to deal with the fusion of different corporates. The huge positive pace that brand India has taken in last few years is very much astonishing. All the sectors, namely, Steel, Manufacturing, IT, Automobile and FMCG are bustling with Mega Indian mergers and acquisitions. The M&A are debatably the most popular strategy among firms who seek to create a competitive advantage over their rivals. Indian Businessmen and Entrepreneurs are set out to restore Indian image as world's biggest corporation's in the future through M&A at different levels in multiple industries. The main corporate objectives behind M&A's are to achieve greater market power, thus maximize efficiency through economies of scale & scope and reform a firm's competitive scope (Hitt et al., 2007). Other reasons encompass a short-term solution to financial problems that companies face due to information asymmetries (Fluck and Lynch, 1999), revitalize the company by bringing in new knowledge to foster long-term survival (Vermeulen and Bakema, 2001) and to achieve synergy effects (Lubatkin, 1987; Vaara, 2002).

This paper investigates the performance of M&A in Indian context by taking an example of Tata Group. The Tata Group is one of the biggest Indian Company to go for multiple mergers and acquisitions over time. This is one of the largest conglomerates in India by market capitalization (USD 100.33 billion) and revenue (US \$83.3 billion) in 2010-11. It has interests in communications and information technology, engineering, materials, services, energy, consumer products and chemicals. The Group has operations in more than 80 countries across six continents. Some of the companies under the umbrella of this group include Tata Steel (including Tata Steel Europe), Tata Motors (including Jaguar and Land Rover), Tata Consultancy Services, Tata Technologies, Tata Tea (including Tetley), Tata Chemicals, Titan Industries, Tata Power, Tata Communications, Tata Sons, Tata Teleservices and the Taj Hotels.

As we know that companies go for M&A for high prospects, but there are contradictory evidences also available, on impact of M&A's on firm's performance. This research paper aims to analyze the post merger & acquisition performance of TATA group during the period 2004-2008. This paper consists of five parts including this introduction section. The second part undertakes literature review. The third part enlists research objectives and explains research design. The fourth part discusses the results and analysis and the last part concludes.

REVIEW OF LITERATURE

There are two main standpoints to measure the performance in the existing M&A literature: the stock-market based approach and the accounting-based approach. The present study undertakes the latter approach to measure the financial performance. Studies based on analysis of accounting data have attempted to assess the economic impact of M&A's by testing for changes in the profitability of the involved companies. In this string of literature, pre-M&A profitability measures are compared to post-M&A profitability measures by parametric tests. Martynova et al. (2007) investigated the long-term profitability of corporate takeovers (both the acquiring and target companies) by using four different measures of performance i.e. (a) (EBITDA - WC) / BVassets (b) (EBITDA - WC) / Sales (c) EBITDA / BVassets and (d) EBITDA / Sales. Where; EBITDA = Earnings before Interest, Taxes, Depreciation and Amortization. This paper stated that the operating profitability of the companies can be calculated by using these measures. Satish et al. (2008), investigated whether the claims made by the corporate sector while going for M&A's to generate synergy, are being achieved or not in Indian context. This is done by evaluating the financial performance on the basis of five parameters i.e. Liquidity position, operating efficiency, overall efficiency, return to equity shareholders and financing composition. The study supports the perception about M&A's that the synergy can be generated in long run with the careful usage of the resources.

Saboo et al. (2009) investigated the performance of Indian companies that have gone through mergers in India and abroad and see if mergers had significant impact on operating financial performance of merging companies by using Pre and Post merger ratios for firms (Debt-Equity Ratio, Long Term Debt-Equity Ratio, Current Ratio and Interest Cover Ratio). E Akben et al. (2011) investigated the impact of M&A deals on the performance of acquirer Turkish companies by using two approaches; Stock market approach and Accounting approach via Return on assets (ROA), Return on equity (ROE) and Return on sales (ROS). Gennaro et al. (2011) investigated the impact of operating synergies on merger performance. The author stated that investor's reaction to mergers varies directly with the availability of these forecasts and post-merger operating performance increases with the predictable component of forecasted synergies based on deal characteristics.

OBJECTIVES OF THE STUDY

The objective of the present research study is to analyze the post-merger financial performance for the companies belonging to the Tata Group during the period 2003-04 to 2007-08. The following are the objectives:

- 1) To study the impact of M&A on financial performance of companies in Tata Group.
- 2) To study whether there is a significant improvement in the financial performance of companies in Tata Group following the M&A deals or not.

RESEARCH HYPOTHESES

To test the objective no.2 mentioned above, the following hypothesis was formulated:

H0: No significant change in the financial performance of the Tata Group in post M&A.

H1: There is a significant change in the financial performance of the Tata Group following the M&A deals.

RESEARCH DESIGN

To study the impact of M&A on financial performance of the company's data for six years has been taken into consideration which includes three years data from Pre-M&A period and three years data post-M&A period of the 24 companies of Tata Group which were involved in the M&A. Further, we have taken Mean pre-M&A & Mean post-M&A Ratios. The data on financial performance ratios has been extracted from CMIE database PROWESS. Researchers have selected year 2003-04 to 2007-08 to identify M&A deals in Tata Group. The reason of selecting this period is that three years post merger performance data is required for the study. Thus, three years pre and post financial ratios are considered for each case; For deals in 2003-04 (pre deal years- 2000-01, 2001-02 & 2002-03 and post deal years include- 2004-05, 2005-06 & 2006-07), for deals in 2004-05 (pre deal years- 2001-02, 2002-03 & 2003-04 and post deal years include- 2005-06, 2006-07 & 2007-08), for deals in 2005-06 (pre deal years- 2002-03, 2003-04 & 2004-05 and post deal years include- 2006-07, 2007-08 & 2008-09), for deals in 2006-07 (pre deal years- 2003-04, 2004-05 & 2005-06 and post deal years include- 2007-08, 2008-09 & 2009-10) and for deals in 2007-08 (pre deal years- 2004-05, 2005-06 & 2006-07 and post deal years include- 2008-09, 2009-10 & 2010-11) are considered to analyze the financial performance of the merging and acquiring companies of Tata Group.

We are conscious of the fact that the accounting-based approach also has problems: Companies can use innovative accounting techniques which may imply that their published accounts may not be a true and fair reflection of the companies' financial position (Dickerson, Gibson & Tsakalotos 1997).

On the other hand, to study whether the post M&A performance of the companies has been improved or not, the post-M&A performance was compared with the pre-M&A performance and tested for significant differences, using "paired sample t-test".

M&A's OF TATA GROUP (2003-04 TO 2007-08)

Year	Number of M&A's of Tata Group	Change (percentage)
2003-04	9	-
2004-05	12	33.33
2005-06	21	75
2006-07	22	4.76
2007-08	13	(40.91)
Total	77	
Within its own Group	32	41.56
With External Companies	45	58.44

Source: CMIE Business Beacon

Table I above depicts that Tata Group entered into 77 M&A's during the period 2003-04 to 2007-08. The total M&A of Tata Group increased to 75% in the year 2005-06 as compared to 33.33% in the financial year 2004-05. During 2006-07 the group again went for M&A of 22 more companies which was around 5% more as compared to the previous year. Out of the total 77 deals, 45 deals (58.44%) were with external companies and 32 deals (41.56%) were within its own group. The researchers have identified 45 companies i.e. where M&A's have taken place with the companies other than the Tata Group. Out of these 45 companies the researchers have selected only 24 companies for this study on the basis of availability of required financial data.

METHODOLOGY

The research study adopted the methodology of comparing pre and post-merger performance of companies in Tata Group, by using various financial ratios for the period 2003-04 to 2007-08. The financial performance is checked on the basis of financial ratios to see the overall financial health of merged and acquired companies. The ratios calculated are: Current Ratio and Debt-Equity Ratio (Saboo et al., 2009), Return on Net Worth and Working Capital (Satish et al., 2008) and Return on Investment (ROI).

- 1) Current Ratio (CR) - To measure a company's ability to pay short-term obligations.
- 2) Working Capital (WC) - To check operating liquidity available for a company.
- 3) Debt-Equity Ratio (D/E) - To get the proportion of equity and debt the company is using to finance its assets.
- 4) Return on Net worth (RONW) - To analyze the profitability from the shareholders' point of view.
- 5) Return on Investment (ROI) - To evaluate the efficiency of an investment.

Pre-M&A and post-M&A financial performance ratios and the averages were computed for the entire 26 deals of sample companies of Tata Group, which have gone through mergers or acquisitions during the period 2004-08. Mean pre-M&A and post-M&A financial ratios were compared for all the five years to see if there was any statistically significant change in financial performance due to mergers and acquisitions, using "paired two sample t-test" at confidence level of 95%.

RESULTS AND ANALYSIS

Analysis of all the mergers and acquisitions (M&A) of Tata Group in the sample for the period of 2003-04 to 2007-08:

The comparison of the pre-M&A and post-M&A financial performance ratios for the entire sample set of M&A of Tata Group during the year 2003-04 (Table I), showed that there was an increase in the mean RONW from 17.92% to 103.9%, but the increase was not statistically significant with t-statistic value of -1.565. RONW is considered as an effective ratio for measuring the overall efficiency of a firm. As the primary objective of a business is to maximize its earnings, this ratio indicates the extent to which the primary objective of the business is being achieved. The ratio reveals how well the resources of the firm are being used, higher the ratio, better are the results.

ROI investigates the magnitude and timing of investment gains directly with the magnitude and timing of investment costs. A high ROI means that investment gains compare favorably to investment costs. There was a statistically insignificant increase in the mean ROI from 15.92% to 79.7%, with a low t-statistic value of -1.715.

The Current Ratio gives a sense of the efficiency of a company's operating cycle. Higher the current ratio, more capable the company is of paying its obligations. The analysis depicts that the mean Current Ratio declined in the post M&A from 13.15 to 4.43 times and this decline was also not statistically significant with a t-statistic value of 0.83.

Debt-Equity Ratio is a measure of a company's financial leverage. A high debt-equity ratio generally means that a company has been aggressive in financing its growth through debt. If a lot of debt is used to finance increased operations (high debt to equity), the company could potentially generate more earnings than it would have without this outside financing. The analysis shows that there was a marginal but statistically insignificant increase in leverage after the M&A from 0.65 to 0.85 times, confirmed by the very low t-statistic value of -1.134.

Working Capital is a measure of both a company's efficiency and its short-term financial health. Positive working capital means that the company is able to pay off its short-term liabilities. Negative working capital means that a company currently is unable to meet its short-term liabilities with its current assets. If a company's current assets do not exceed its current liabilities, then it may run into trouble paying back creditors in the short term. The mean working capital showed a statistically insignificant increase in the post M&A from Rs. 225.4 Millions to Rs. 12039.95 Millions with t-statistic value of -1.806.

The result suggests that there was insignificant increase/decrease in the financial performance of Tata Group from all M&A's during the year 2003-04 except the Debt-Equity Ratio which increased significantly. Based on the results, **the alternative hypothesis (H1) i.e. there is a significant change in the financial performance of the Tata Group following the M&A deals, was rejected.** Since, an insignificant increase/decrease was found after the statistical analysis of the pre and post financial ratios of the M&A deals.

The comparative analysis of the pre-M&A and post-M&A financial performance ratios for the entire sample set of M&A of Tata Group during the year 2004-05 (Table II), showed that there was a statistically insignificant increase in the mean RONW from 37.04% to 114.89% with a t-statistic value of -2.302 and ROI from 21.76% to 76.69% with a t-statistic value of -4.577. Mean Current Ratio declined in post M&A from 9.31 to 3.39 times and this decline was statistically insignificant with a t-statistic value of 0.916. The analysis shows that there was a statistically insignificant decrease in Debt-Equity Ratio after the M&A from 3.9 to 1.29 times, confirmed by the t-statistic value of 1.161. The mean working capital showed a statistically significant decrease in the post M&A from Rs. -27196.43 Millions to Rs. -74444.03 Millions with a t-statistic value of 4.894.

The results suggest that there was both an increase/decrease in the financial performance of Tata Group from all M&A's. All the ratios increased/decreased insignificantly except Working Capital (decreased significantly). Therefore, **the alternative hypothesis (H1) was rejected.** An insignificant transformation was found after the statistical analysis of the M&A deals.

The results of the pre-M&A and post-M&A financial performance ratios comparison for the entire sample set of M&A of Tata Group during the year 2005-06 (Table III), showed that there was an increase in the mean RONW from 53.01% to 60.9%, and the increase was not statistically significant with a t-statistic value of -0.274. There was also an increase in the mean ROI from 38.12% to 43.97%, and the increase was statistically insignificant with a t-statistics value of -0.325. The analysis depicts that the mean Current Ratio declined in the post M&A from 3.49 to 2.96 times and this decline was not statistically significant, t-statistic value of 0.681. The analysis also shows that there was a statistically insignificant decrease in the Debt-Equity Ratio after the M&A from 1.67 to 1.64 times, confirmed by the t-statistic value of 0.082. The mean working capital showed a statistically insignificant decrease in the post M&A from Rs. -14042.8 Millions to Rs. -47292.84 Millions with t-statistic value of 2.2.

The result suggests that there was an insignificant change in the financial performance of Tata Group from all M&A's during the year 2006-07. Therefore, **the alternative hypothesis (H1) was rejected.** An insignificant change was found after the statistical analysis of the M&A deals.

The comparative analysis of the pre-M&A and post-M&A financial performance ratios for the entire sample set of M&A of Tata Group during the year 2006-07 (Table IV), states that there was a statistically insignificant decrease in the mean RONW from 82.53% to 44.46% with a t-statistic value of 2.303. The ROI also decreased from 50.21% to 35.64% and the decrease is statistically insignificant with a t-statistic value of 1.923. There was a statistically insignificant increase in the Mean Current Ratio from 8.7 to 15.99 times with t-statistic value of -0.741 and Debt-Equity Ratio after the M&A from 3.2 to 4.35 times with a t-statistic value of -1.402. The mean working capital showed a statistically insignificant decrease from Rs. -18120.98 Millions to Rs. -51657.56 Millions with a t-statistic value of 2.661.

The results suggest that there was both an increase/decrease in the financial performance of Tata Group from all M&A's. RONW, ROI and Working Capital decreased whereas, Current and Debt-Equity Ratio increased insignificantly during the year 2006-07. Therefore, **the alternative hypothesis (H1) was rejected.** An insignificant variation was found after the statistical analysis of the M&A deals.

The analysis of the pre-M&A and post-M&A financial performance ratios for the entire sample set of M&A of Tata Group during the year 2007-08 (Table V), showed that there was a statistically insignificant increase in the mean RONW from -62.24% to 15.2% with a t-stats value of -0.902. The ROI decreased from 15.01% to 6.97% and the decrease was statistically insignificant with a t-statistic value of 1.77. The Mean Current Ratio declined in post M&A from 4.99 to 2.25 times and this decline was statistically insignificant with a t-statistic value of 1.672. There was a statistically insignificant increase in Debt-Equity Ratio after the M&A from 0.94 to 1.01 times with t-statistic value of -0.819. The mean working capital showed a statistically insignificant decrease in the post M&A from Rs. -975.08 Millions to Rs. -14937.13 Millions with a t-statistic value of 2.43. The results suggest that there was insignificant increase/decrease in the financial performance of Tata Group from all M&A's during the year 2007-08. Therefore, **the alternative hypothesis (H1) was rejected.** Insignificant changes were found after the statistical analysis of the M&A deals.

CONCLUSION AND SUGGESTIONS

This study was undertaken to test whether there is any significant changes in the financial performance of Tata Group from all the M&A's during the time period 2003-04 to 2007-08. The results from the present study of the pre and post M&A financial performance ratios of the Tata Group reveals that there was no significant increase/decrease in the financial ratios. This means that M&A's in Tata Group has not significantly affected Tata Group's financial performance.

The results must be considered in light of the following limitations. First, the period examined in this study is only three years for post acquisition period. This may not seem adequate for gains to materialize following an acquisition, however as explained in the paper, extending the post-acquisition period would cause sample size problems. Second, the accounting measures used in this study were based on net income rather than on pure cash flows. Hence, they might be affected by taxation, depreciation methods etc. Future research could extend the literature on M&As of Tata group by addressing these limitations as well as the cause behind this phenomenon.

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ANNEXURE

ANNEXURE 1

LIST OF TATA GROUP'S M&A'S USED IN THE STUDY (2003-04 TO 2007-08)

S. No.	Target/Seller Co.	Merged/Acquirer Co.
1	21st Century Infra Tele Ltd.	Tata Teleservices (Maharashtra) Ltd.
2	Geodynamics Ltd.	Tata Power Co. Ltd.
3	Direct Internet Ltd. [merged]	Tata Communications Internet Services Ltd.
4	General Chemical Indl. Products Inc.	Tata Chemicals Ltd.
5	Indian Hotels Co. Ltd.	Tata Investment Corporation. Ltd.
6	Praj Industries Ltd.	Tata Sons Ltd.
7	Development Credit Bank Ltd.	Tata Capital Ltd
8	Mount Everest Mineral Water Ltd.	Tata Global Beverages Ltd.
9	Automobile Corporation. Of Goa Ltd.	Tata Motors Ltd.
10	Coastal Gujarat Power Ltd.	Tata Power Co. Ltd.
11	P T Arutmina Indonesia	Tata Power Co. Ltd.
12	Rawmet Ferrous Inds. Ltd.	Tata Steel Ltd.
13	Corus Group Plc	Tata Steel U K Ltd.
14	Joekels Tea Packers C C	Tata Global Beverages Ltd.
15	Gharda Chemicals Ltd.	Tata Chemicals Ltd.(proposed)
16	Indigene Pharmaceuticals Pvt. Ltd.	Tata Industries Ltd.
17	Eight'o Clock Coffee Holdings Inc	Tata Coffee Ltd.
18	Direct Internet Ltd. [merged]	Tata Communications Ltd.
19	Cedis Mechanical Engg. Gmbh	Tata Motors Ltd.
20	Airline Financial Support Services (india) Ltd. [merged]	Tata Consultancy Services Ltd.
21	Hispano Carrocera Sa	Tata Motors Ltd.
22	Telco Dadajee Dhackjee Ltd.	Tata Motors Ltd.
23	Highhill Coffee India Pvt. Ltd. [merged]	Tata Coffee Ltd.
24	W T I Advanced Technology Ltd.	Tata Consultancy Services Ltd.

ANNEXURE 2

(TABLE I: MEAN PRE-M&A AND MEAN POST- M&A RATIOS OF THE SAMPLE FIRMS OF TATA GROUP (2003-04)

M&A's during 2004	Pre-M&A (2000-01 to 2002-03)	Post-M&A (2004-05 to 2006-07)	t-value (0.05 significance)
Return on Net Worth	17.92	103.9	-1.565
Return on Investment	15.92	79.7	-1.715
Current Ratio	13.15	4.43	0.83
Debt-Equity Ratio	0.69	0.85	-1.134
Working Capital (Rs. Millions)	225.4	12039.95	-1.806

TABLE II: MEAN PRE-M&A AND MEAN POST- M&A RATIOS OF THE SAMPLE FIRMS OF TATA GROUP (2004-05)

M&A's during 2005	Pre-M&A (2001-02 to 2003-04)	Post-M&A (2005-06 to 2007-08)	t-value (0.05 significance)
Return on Net Worth	37.04	114.89	-2.302
Return on Investment	21.76	76.69	-4.577
Current Ratio	9.31	3.39	0.916
Debt-Equity Ratio	3.9	1.29	1.161
Working Capital (Rs. Millions)	-27196.43	-74444.03	4.894

TABLE III: MEAN PRE-M&A AND MEAN POST- M&A RATIOS OF THE SAMPLE FIRMS OF TATA GROUP (2005-06)

M&A's during 2006	Pre-M&A (2002-03 to 2004-05)	Post-M&A (2006-07 to 2008-09)	t-value (0.05 significance)
Return on Net Worth	53.01	60.9	-0.274
Return on Investment	38.12	43.97	-0.325
Current Ratio	3.49	2.96	1.316
Debt-Equity Ratio	1.67	1.64	0.082
Working Capital (Rs. Millions)	-14042.8	-47292.84	2.2

TABLE IV: MEAN PRE-M&A AND MEAN POST- M&A RATIOS OF THE SAMPLE FIRMS OF TATA GROUP (2006-07)

M&A's during 2007	Pre-M&A (2003-04 to 2005-06)	Post-M&A (2007-08 to 2009-10)	t-value (0.05 significance)
Return on Net Worth	82.53	44.46	2.303
Return on Investment	50.21	35.64	1.923
Current Ratio	8.7	15.99	-0.741
Debt-Equity Ratio	3.2	4.35	-1.402
Working Capital (Rs. Millions)	-18120.98	-51657.56	2.661

TABLE V: MEAN PRE-M&A AND MEAN POST- M&A RATIOS OF THE SAMPLE FIRMS OF TATA GROUP (2007-08)

M&A's during 2008	Pre-M&A (2004-05 to 2006-07)	Post-M&A (2008-09 to 2010-11)	t-value (0.05 significance)
Return on Net Worth	-62.24	15.2	-0.902
Return on Investment	15.01	6.97	1.77
Current Ratio	4.99	2.25	1.672
Debt-Equity Ratio	0.94	1.01	-0.819
Working Capital (Rs. Millions)	-975.08	-14937.13	2.43

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