CHAPTER 1

INTRODUCTION

1.1 New Industrial Policy 1991 and Corporate Restructuring in India

The 1990s have experienced a significant change in Indian industrial environment. The Government of India has initiated a series of economic reforms in the 1990s. Relaxation of government controls or doing away with controls altogether has been an important and integral part of this strategy which came to be epitomised as economic liberalization (for differing views on liberalization see Guha (1990: 3-4) and Nayyar (1996)). One of the significant reforms was the declaration of a New Industrial Policy (NIP) (refer to Vaidyanathan (1995: x), Glen and Pinto (1994: 48); Basu (1993); Guha (1990: 3, 4); Industrial Development — Global Report (1995: 97) and Rastogi (1994)) in July 1991, which envisaged a radical change in government orientation towards industrial policies through the liberalization objectives, with a view to raise industrial efficiency to the international level and, mainly through it, accelerate growth. The NIP, 1991, with its overall liberalization and globalization thrust was a major change to which the industrial structure in India was expected to respond. With a shift in India's policy position from a protectionist regime to a so-called liberalized one, the change was apparently, in terms of the opening up of the economy to internal as well as external competitive forces. Since the liberalization in 1991 and the adoption of the NIP and associated measures, certain trends in the behaviour of firms have become distinctly discernible, which the firms have been resorting to, as alternative strategies for corporate repositioning. Some of them are:

* Corporate restructuring in the form of business consolidation and reorganisation within the industries or across, along synergistic lines and increasingly taking the route of mergers, takeovers (TOs), acquisitions, strategic alliances and other types of amalgamations, leading to changes in ownership structures and struggles for corporate control.

* Setting up of collaborations/product-specific joint ventures with foreign collaborators becoming widespread.

* The Indian companies encouraging foreign direct investment in a big way.

* Domestic firms expanding with Euro-issue shares.

* Foreign parent companies increasing their equity in their Indian subsidiaries through the subsidiaries transferring shares to their foreign holding companies at a preferential price to pave the way for foreign parent companies to raise their equity holding in the Indian companies.
* Domestic firms raising money by privately placing shares with Foreign Institutional Investors (FIIs) to face competition;

* Consumer goods industries experiencing maximum amount of activities, specially in the segment that caters to the middle to upper income groups; introduction of new brands as well as competitive extension of mother brands becoming common practice.

The thesis concentrates on corporate restructuring activities in the form of the recent amalgamation, merger and TO activities in the manufacturing sector in India. The post-liberalization era in India is marked by a series of fiscal, financial and legal reforms. In general, the currently pursued governmental policies initiated through the NIP 1991, have opened up the potentials for competition through larger inflow of new domestic entrants, through expansion of existing undertakings as well as through the entry of the multi-national companies (MNCs). The increased role of the stock market, de-licensing policy, abolition of the MRTP and FERA restrictions, especially the pre-merger scrutiny by the MRTP Commission, and the availability of a large number of sick and weak firms in the 1990s have opened up possibilities of restructuring both at the firm level and at the level of industry. This restructuring can take place in the form of different kinds of expansionary activities through new investments as well as through merger and TO activities and other types of corporate fusion activities, resulting from the desire of particular business groups to expand in existing lines, enter areas with strategic possibilities and/or shed some activities as a part of the restructuring process in response to liberalization.

There are cases of horizontal, vertical as well as conglomerate unification activities taking place in the Indian industries. There are also cases of unification between sick and healthy companies under the rehabilitation scheme of the Board of Industrial and Financial Reconstruction (BIFR) as also under the form of reverse mergers and integrations. Mergers and acquisitions and associated industrial restructuring have raised important issues both for business decisions and for public policy formulation. It is therefore necessary at this juncture to provide a detailed study of the mergers and acquisitions in India in the nineties in terms of the nature, causes and effects of such corporate fusion activities.

1.2 The Extent of Merger and TO Activities in India in the Post-Liberalization Regime

The mergers and acquisitions observed in India are many and diverse with different activating factors for domestic and foreign firms and also for domestic firms. Such mergers and TO activities may be broadly as follows:

(a) a domestic firm of a group taking over (and perhaps at some later date merging with) another domestic firm of another group;
(b) a domestic firm being taken over (and occasionally taking over) by a foreign firm;

(c) firms of the same business group, whether Indian, or subsidiaries of foreign parent companies, merging to avoid overlapping of activities and hence to take advantage of economies of scale through horizontal/vertical integration;

(d) healthy firm taking over a sick firm, both of which may or may not belong to same parent firm;

(e) sick firm merging with it a healthy firm into a reverse merger;

(f) an Indian firm taking over a foreign firm.

Table 1.1 shows the number and percentage change in the number of merger and TO activities in India from 1988 to 1998. These mergers and TOs include the realised as well as abortive bids. Table 1.1 exhibits a sharp rise in the overall merger and acquisition activity in the Indian corporate sector. While there were 58 mergers and TOs from 1988 to 1990, the number rose to 71 in 1991 and 730 in 1998. There was a jump in the number of merger and TO activities in India from 1988 to 1993, the average rate of increase being around 89% for the five-year period. Since then the rate of rise had maintained an average of 20.5%. Khanna (1998: 10) has referred this situation in India as the “first merger wave” in India.

### Table 1.1

<table>
<thead>
<tr>
<th>Year</th>
<th>Number</th>
<th>Change (%)</th>
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</thead>
<tbody>
<tr>
<td>1988</td>
<td>15</td>
<td></td>
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<tr>
<td>1989</td>
<td>18</td>
<td>20.0</td>
</tr>
<tr>
<td>1990</td>
<td>25</td>
<td>38.9</td>
</tr>
<tr>
<td>1991</td>
<td>71</td>
<td>184.0</td>
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<tr>
<td>1992</td>
<td>135</td>
<td>90.1</td>
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<tr>
<td>1993</td>
<td>288</td>
<td>113.3</td>
</tr>
<tr>
<td>1994</td>
<td>363</td>
<td>26.0</td>
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<tr>
<td>1995</td>
<td>430</td>
<td>18.5</td>
</tr>
<tr>
<td>1996</td>
<td>541</td>
<td>25.8</td>
</tr>
<tr>
<td>1997</td>
<td>636</td>
<td>17.6</td>
</tr>
<tr>
<td>1998</td>
<td>730</td>
<td>14.8</td>
</tr>
</tbody>
</table>

Source: Collated from various newspapers including business dailies, various issues and also “Monthly Review of the Indian Economy”, CMIE, various issues.
Table 1.1 presented above shows the number of merger and TO “announcements” over 1988 and 1998. These announcements were made in a number of newspapers including business dailies and also the CMIE bulletin “Monthly Review of the Indian Economy”. Each pair of firms (target and bidder) is treated as one announcement. However, if a firm has more than one bidder and the press reports these bidders at different points of time, our data-base will have multiple entries. This provides for some firms appearing in the data-base more than once. One such example would be the case of Ahmedabad Electricity Company for which the Torrent group made the first bid and the subsequent bid was made by Bombay Dyeing. This led to an imbroglio after which the Torrent group could finally acquire Ahmedabad Electricity Company [1]. Our data records all merger and TO announcements irrespective of size. A large number of consolidations in our data-base pertain to small investment firms used by Indian business groups to maintain control over their own firm. In contrast, the acquisitions made by foreign companies are of relatively large sized firms.

The trend of rising merger and acquisition activities in the 1990s is not surprising as the industrial deregulation has led many Indian firms to restructure their businesses in mainly two ways:

• re-assessing their “line of business” decisions
• merging numerous corporate entities within the group, often with similar or overlapping businesses, which were hitherto all held as separate corporations to avail of the tax concessions, or cheaper financing etc.

So far as the first option is concerned, the large business houses exit some industries where they had strayed because of availability of license and where future returns became uncertain due to entry of foreign firms or competitive situation. This has been done through sale of companies or creation of new corporate entities to be spun off and ultimately divested as promoters selected their lines of business and focused on a narrow range of economic activities. On the other hand, those who bought this business did so presumably because they felt that they were in a better position to manage it, or to prevent it from falling into the hands of a rival firm in the industry.

The second route, that is the one of mergers, requires absorption of one or corporations into another corporate body, to create larger corporations. This is done to tap the financial and operational synergies. The argument is that in India, several industries are fragmented with industry capacity broken up into independent small or medium size firms, each lacking economies of scale. Consolidation of this capacity was expected to lead to lower costs or other advantages that are derived from larger scale operations. Similarly, merger of group companies meant that the new entity could in the post-merger situation, have a stronger balance sheet, better credit rating and could raise debt at lower cost.

The opening up of the Indian economy to foreign capital along with the abortion of industrial licensing has also attracted a substantial number of MNCs and provided a spurt in corporate consolidation activities. In addition, the opening up of the infrastructure sectors, till now monopolised by the Indian public sector, has brought
in a number of MNCs in power, telecom etc. In these sectors, the Indian private sector firms are either absent or weak.

Some significant examples of the recent merger and acquisition activities in the manufacturing sector are the acquisition of Tata Oil Mills Company (Tomco) of the Tata group by Hindustan Lever Limited (HLL), the disappearance of Parle of the Chauhans as a soft drinks manufacturer in the hands of Coca Cola and the acquisition of ACC Babcock by Asea Brown Boveri Limited (ABB). Kwality of the Wigs and Kissan of Vijay Mallya have managed to remain but under a new ownership, namely, that of HLL. Incidentally, it appears from all these cases referred to, that the large international firms are always the raiders. However, there are similar examples of mergers, acquisitions and TOs by domestic firms too. In the case of mergers, we may cite the examples of the amalgamation of Miami Pharma with Lakme Ltd. in the consumer product sector, the merger of Indian Hard Metal with Shriram Industrial Enterprises in the machinery sector, the merger of Hyderabad Allwyn Ltd. with Voltas Ltd in the electrical equipment (white goods) sector, etc. where in each case, both the firms are domestic ones. However most of these mergers between different industrial groups fall under the rehabilitation scheme of BIFR. In TOs, we find the acquisition of Radiant Electronics Ltd. by Crompton Greaves Ltd. in the telecommunications sector, Merind Ltd by Wockhardt in the pharmaceutical sector, or the TO of Utron Colour Picture Tubes by BPL Ltd. in the electronics sector as similar examples where both the acquiring and acquired companies are domestic.

Apart from mergers and acquisitions in the manufacturing sector, there are also consolidations taking place between firms in the financial sector. The acquisition of ITC Classic Finance of ITC and also Anagram Finance the Lalbhai group by Industrial Credit & Investment Corporation of India (ICICI), Empire Finance by Ranbaxy group etc. are a few such examples. Also there has been a number of mergers between private banks over this period. Some of the instances are the ingroup mergers between Chetana Co-operative Bank and Rupee Co-operative Bank, Bareilly Corporation Bank and Bank of Baroda etc. or the outright sale of Punjab Cooperative Bank and Baridoav Bank to Oriental Bank. There have also been corporate consolidations in a number of service and service-related sectors.

We will however concentrate on the merger and TO activities in India in the nineties in the manufacturing sector only. This is because the merger and TO in the manufacturing sector is supposed to have direct effect on the economic health of the country whereas the corporate consolidation activities outside the manufacturing sector such as finance, service and related sectors have their effect on the economy through indirect linkages only. Since we are more inclined to know to what extent the corporate restructuring in India in the nineties have directly affected the texture of the economy we restrict our analysis to the manufacturing sector only.

1.3 Period of Study

In general, the study covers mergers and acquisitions in the Indian corporate sector in the post-NIP regime. We will concentrate specifically on the merger and TO activities that have occurred in India over the period 1994 to 1998. However, for a meaningful
and detailed analysis of mergers and acquisitions we have, wherever necessary also looked into the period before 1994.

It is interesting to note that the two terminal periods, 1993-1994 and 1997-98 for our set of mergers and TOs, appear to be significant. This is reflected in the following ways. Mergers and TOs in India gradually started to get due importance and recognition at the national policy level, as reflected by the formulation of the Sebi Regulations on Substantial Acquisition of Shares and TOs, 1994 (Sebi (Substantial Acquisitions of Shares & TOs) Regulations, 1994) as also by the government decisions to bring about changes in company laws governing mergers. Table 1.1 above shows that the number of mergers and acquisitions increased from 33 in 1991 to 114 in 1993 and 150 in 1994. The figure indicates that there was a massive (354.5%) jump in the number of amalgamation activities from 1991 to 1994. In fact, there has been a structural shift in the number of mergers and acquisitions from 1993. Increase in the number of TOs is an index of the increase in the volume and transaction of capital market. It is quite natural that this massive increase had led Sebi to the restructuring of TO laws.

1997 and 1998 were also remarkable from the point of view of Sebi regulations on TO activities in our country (Sebi (Substantial Acquisitions of Shares & TOs) Regulations, 1997; Sebi (Substantial Acquisitions of Shares & TOs) Amendment Regulations, 1998). The importance of 1997 lies in the fact that the revised TO Code was notified in February 1997, reportedly being triggered by the two contemporary hostile TO bids -- the Torrent versus Bombay Dyeing bid for Ahmedabad Electricity Company, and the NEPC-Modiliuft imbroglio. The revised code was considered to be a remarkable effort as it marked at least theoretically an effort to recast the legal and regulatory arrangements governing mergers and acquisitions in India, by incorporating the ideas of hostile TO bids, competitive bids etc. in the Sebi TO code, at a juncture where there was a visible trend towards the development of an active market for corporate control. The Sebi amendment regulations on TOs was notified in October 1998.

1.4 Data Source and Methodology, Sampling

1.4.1 Data source and Methodology

Data Source
At the different stages of the analysis, different secondary data sources have been exploited. There are two distinct types of data used in this thesis. One is the general economic data projecting the overall economic environment in India following the initiation of liberalization. For this we have resorted to various governmental publications like the Company News and Notes, a publication of the Department of Company Affairs (DCA), Report on Currency and Finance of the Reserve Bank of India, Economic Survey, etc. and also the various business newspapers (Economic Times, Statesman, Telegraph) and business journals (Business Standard, Business Today, Business India, Dalal Street Journal etc.). Apart from this, there is an extensive analysis of the causes and consequences of the specific merger and TO
activities in India over 1994-98 in 15 sectors of the economy. For this, we have used firm-level data on various financial variables. We have used the balance sheets and profit and loss accounts of the relevant companies, available from the Bombay Stock Exchange Directories. We have also procured such data from the newspapers and business journals mentioned above.

In statistical data analysis the source of firm-level data has mainly been several annual issues of Business Standard, an Indian financial journal which comes out as supplement to the daily business newspaper by the same name and contains financial information on a large number of Indian companies. These annual issues have been presenting the annual data on a number of financial aggregates and ratios of the top 1000 Indian companies ranked on the basis of net sales since 1993 till 1998 (prior to this, the data provided by Business Standard was over 300 companies). These top 1000 companies are spread across manufacturing, transport and services sector across all patterns of ownership. The financial and banking firms have been excluded from the compilation and analysis of Business Standard. The data provided by Business Standard has been computed from the audited annual reports (balance sheets as well as well profit and loss accounts) of companies.

One reason for selecting Business Standard was that it is one of the very few Indian business journals that offers the annual data base for top 1000 companies whereas the others do the same for 100, 300 or 500 companies. Taking 1000 companies as the population has allowed us to secure data for many companies not available elsewhere. In spite of this, we have not been able to obtain data for many other companies engaged in mergers and acquisitions. Apart from this we have also used the “ET 500” data base of Economic Times, wherever required to supplement and complement the data base of Business Standard. In spite of our earnest effort, we have not been able to obtain data for many other companies engaged in mergers and acquisitions.

The corresponding industry data used in Chapter 8 to compute a measure of market concentration has been compiled from the 1998 and 1999 issues of the “Industry Financial Aggregates and Ratios” of CMIE. The CMIE data is reported to have been derived from the Annual Survey of Industries (ASI) and from the company annual reports. The CMIE sample selected is based on the availability of the unaudited unabridged annual accounts of the manufacturing companies. The coverage includes public sector (restricted by availability mostly to central government public sector enterprises, cooperatives and joint stock companies. The sample includes listed as well as unlisted companies (CMIE (1999)).

Methodology
The analysis is mainly carried out using analytical and classificatory exercises and case-studies. The specific methods employed are stated in the relevant chapters.

1.4.2 Sample

A serious handicap in the sample selection was the lack of availability of a comprehensive list of mergers and TOs in India for 1994-98. No comprehensive data
on the merger and acquisition activity is available in India. The Bombay Stock Exchange publishes a list of the mergers only and not the TOs. Apart from this limitation, the most recent list of the Bombay Stock Exchange available to us at the time of drawing the sample cases was of the period 1988-1996. The information-base on mergers provided by the Bombay Stock Exchange was thus only partially helpful. The CMIE publishes monthly data both on mergers and TOs. But the CMIE data is available from September 1995. We have made efforts to fill the gap by compiling a comprehensive list of such acquisitions during the 1994-98 period. Much of the information on merger and acquisition activities for our period had to be drawn from various secondary sources like the various newspapers and journals mentioned above. Though all attempts to include all the cases has been made through a scrutiny of secondary sources, no claim about its scope is made.

On the basis of the different information sources mentioned above, we had first made an exhaustive list, of 839 cases comprising 185 mergers and 558 TOs of different kinds (the varieties of TOs are mentioned in Chapter 3) plus 96 open offers that have actually materialised in India over 1994-1998. The list was compiled by resorting to a method of listing the consolidations among all the announcements that were reported in newspapers and journals over the period. This list included companies engaged in manufacturing, banking, financial, service, mining, electricity, hotels, entertainment etc. The coverage included mainly private sector companies and a few public/joint sector companies, where the latter has incidentally become a party, generally a target in corporate unification activities. The list included listed and unlisted companies.

In the next step, we have performed a classificatory exercise, as far as practiceable, on this preliminary list of mergers and TOs in a couple of steps based on certain screening procedure, so as to generate a comprehensive sample of merger and TO activities in India, in the manufacturing sector only over 1994 to 1998. The details of the classificatory exercise have been elaborated in Chapter 3.

Apart from the mergers and TOs, recorded in our list, there is a set of 96 open offers for the target companies. Some of these open offers that have actually materialised have been taken care of in our final list in Appendix 3.1, under the appropriate forms of TOs. The other open offers that have not materialised over 1994-98 have been listed under “TO—open offers” in our final list, for record purpose only [2].

1.5 Plan of the Study and Chapter Design

The major issues regarding corporate amalgamation and mergers, acquisitions and TOs, which will be addressed in this thesis are the different aspects of definition, nature, structure and composition of mergers and TOs, the causal factors operating behind them, their effects mainly in terms of market concentration and also in terms some other indicators of corporate performance and well-being, and also certain CG aspects associated with mergers and TOs in India. Accordingly the chapters have been arranged in the following manner. While we provide an overview of the problem in this chapter, Chapter 2 provides a survey of the existing economic literature on mergers, acquisitions and TOs covering the conceptual, causal and performance-related dimensions of such fusion activities. In Chapter 3, we discuss the
nature, structure and composition of the contemporary mergers and TOs in India. A characterisation of the nature of the acquiring and acquired firms in India in terms of certain indices such as size, net worth, capital structure and profitability has been attempted in this chapter. Chapters 4 to 7 concentrate on the causal aspects of the contemporary mergers and TOs in the country. The usual economic and non-economic factors motivating mergers and TOs in India are discussed in Chapter 4. The issue of liberalization, its effects on the stock market and resultant merger and TO activities is taken up for discussion in Chapter 5. In Chapter 6, we discuss the effect of liberalization on foreign investment and the resulting effect on corporate consolidation in India in the 1990s. The other policy-based causal factors operating behind mergers and TOs in India are analysed in Chapter 7. In Chapter 8 we proceed to discuss the effect of mergers and TOs in India in terms of market concentration and firm-profitability. Certain issues of CG structure, proposals and policies in India associated with mergers and TOs are discussed in Chapter 9. Chapter 10 is the concluding chapter of the thesis where we point out the major findings of this study, the main policy implications and possible areas of further research in this extremely wide field of study of the mergers and TOs in India in the post-liberalization regime. The last section consists of the data appendices of various chapters.

The scope for analysis of the behaviour of mergers and TOs in India in the post-liberalization period is infinite and full justice to the possibilities would merit a voluminous work on the subject. We have, however, limited our analysis to only a broad survey of the nature, causes consequences and policy implications of merger and acquisition activity in our economy in the liberalized era, in the backdrop of the merger and TO policies in India.

   Also refer to:


2. Although we will not discuss the unrealised open offers in our thesis, we need to mention an important point with regard to TOs in the form of open offers. The Sebi clause for an open offer to the general shareholders vide the Sebi Regulations 1997 on Substantial Acquisitions of Shares and TOs holds that if the acquirer acquires more than 10% shares in a company, he has to make public announcement of offer to buy additional 20% shares from public at a price not lower than open market price in the last six months. Such an offer would provide option to existing shareholders to sell their shares if they do not have the confidence in the likely new management. The public announcement should contain details as prescribed in the regulations of the Sebi guidelines on TOs. The offer must be kept open for at least six weeks. This clause applies to any buyer (even the promoter who wants to increase his stake) who has taken over the controlling stake of a company, as per Clause 40A and 40B of the listing agreement. But, there are situations when nobody is actually taking over the controlling stake of the company; it is instead being sold under the directive of the Supreme Court. In such cases, Sebi clause for TOs need not apply. An example of such TO in India is that of Eveready Industries India Limited by McLeod Russell in 1996. TOs through open offers extend good exit options for the minority shareholders of the target companies, as the offer is at a price higher than the prevailing price of the scrip.