Summary of Findings and Suggestions

Findings of the Study

Conclusions and Suggestions

Suggestions for Future Research
Till the early nineties, Indian economy functioned in a controlled and regulated environment. With the reforms initiated by the government (namely, amendment in MRTP Act, 1969 to facilitate expansion of an enterprise, amendment in FERA, 1973 to permit direct foreign investment and abolition of industrial licensing in most of the industries), the economy transitioned from “controlled” to market driven and competitive environment. This liberalization of the earlier state controlled sluggish economy forced Indian industries to undergo the process of restructuring in order to gain competitive strength, both in domestic and export market.

The present business environment is characterized by globalization, opening up of economy, would wide competition, expanding markets, fast changing technologies, never ending need for finance and necessity of diversification etc. The Indian Corporate World, while benefiting from decontrol and deregulation has begun to, feel the effect of these competition, Indian corporate are changing their strategic focus and restructuring their businesses by adopting tools like mergers, acquisitions and strategic alliances. Now, s-mall is no longer beautiful in the field of business, trade and commerce. The focus is on larger business establishments to achieve efficiencies and to stand up against global in challenges and worldwide competition by availing economies of scale. This has resulted in “Merger Wave” in India and abroad. Various business establishments and multinationals are expanding by means of mergers and acquisitions.
A number of studies have been carried out on this burning topic abroad especially in the developed capital markets of U.S. and U.K. These studies have covered various aspects, viz., (a) financial performance evaluation of the merged firms using share price data and accounting data, (b) motives of mergers and their empirical investigation, (c) examination of financial characteristics of merged and merging firms and (d) determination of aggregate merger activity.

M & As being relatively less popular phenomenon in India has not received much attention of researchers. The present study is aimed at examining the M&A activity in India during the post-liberalisation period in terms of its financial performance. An attempt has also been made to evaluate the pre- and post-merger performance.

This concluding chapter of the study is mainly devoted to the discussion of its main findings. The chapter is divided into four sections. Recapitulates the methodology followed in the study. Next part enumerates the main findings of the study, its conclusion and summarized in last part of this chapter followed by suggestions for further research.

OBJECTIVES AND RESEARCH METHODOLOGY

The study had the following objectives:

1. To evaluate the post-merger performance of merged firms using the value added metrics namely EVA, MVA and RONW.

2. To identify the motives of mergers and acquisitions as avowed in the merger schemes and to assess if motives as avowed in the scheme have been fulfilled of not.
3. To evaluate the pre-and post-merger financial performance of merged firm’s vis-a-vis the influence of motives’ variables such as:
   a) Profit maximization
   b) Growth
   c) Tax Consideration
   d) Diversification
   e) Leverage

For achieving these objectives, the study focused on three main aspects, viz., (a) evaluation of post-merger performance in terms of value addition to shareholders, (b) examination of motives as avowed in the merger schemes and (c) pre- and post-merger motives’ analysis. It is reiterated that methodology followed for each of these aspects was different. It is therefore useful to briefly recapitulate the methodology followed in the study. In the first aspect, post-merger performance of companies which merged during the year 1999-2000 was analyzed in terms of value addition to shareholders. For this purpose, value added metrics namely EVA, MVA and RONW were computed for three post-merger years for a sample of two hundred and twenty three companies whose financial data was derived from CMIE. Further, inter-firm analysis and inter-industry analysis were conducted using the correlation analysis.

The second aspect was related to an in-depth pre-and post-merger financial analysis in terms of motives of merger to assess if, motives as avowed in the merger schemes have been achieved or not. Five variables were defined as motives of mergers, namely, profitability, tax advantage,
and growth of assets. These variables were empirically calculated with the help of ratios for the sample of fifty six merged firms for a period of three years preceding the merger and compared with value of these variables motives on value addition to shareholders in the post-merger period was also established.

The following null hypotheses were tested in the study:

1. Mergers and acquisitions do not result in value addition to existing shareholders
2. Merger in India is not predominantly horizontal.
3. There is no difference between pre- and post-merger performance of merged companies under the study period.
4. Synergy in profits, acquisition of market share, tax consideration and diversification, all do not result in value addition to existing shareholders.
5. There is no significant difference in the value addition to the existing shareholders due to Growth and Leverage.
6. Motives as avowed in the merger schemes have not been affected after mergers.

FINDINGS OF THE STUDY

With the transition of Indian economy to a competitive and market driven environment, M&A activity has gained momentum, both, in terms of number and volume. Shareholder value addition and survival of the fittest are the buzz words.
The corporate sector has increasingly resorted to consolidations in the form of mergers in order to achieve motives of increased synergies and economies scale, achieve global competitive strength, acquire better marketing and financial advantages, diversify and reduce earnings’ variations, increasing domestic share, enhance production capacities and capture fast growing markets abroad.

The findings of the study are discussed under three major heads, viz., (a) post-merger performance evaluation in terms of value addition of shareholders, (b) merger scheme analysis and (c) competitive pre-and post-merger motives’ analysis.

Post-merger Performance Evaluation

As stated earlier, post-merger performance of fifty six sample merged firms was examined with the help of value added metrics, namely, EVA, RONW, and MVA. Statistical techniques of cluster analysis were employed to analyse and interpret the results. The null hypothesis that mergers do not result in value addition to shareholders has been accepted and alternate hypothesis that mergers add to shareholders’ value has been rejected. The findings of the analysis are summarised in five categories as follows:

A. Intra-company Analysis

1) Cross sectional analysis of sample merged firm in terms of EVA revealed that 79% of the firms resulted in value erosion for its shareholders with decreasing, or no visible trend in three post-merger years. Only 21% of firms exhibited positive value for shareholders who increased in these years. Zenith Infotech
Limited, Arvind Products Limited, NLC Nalco India Limited, IFGL Refractories were few companies gained in post merger period.

2) Similar analysis carried on with the traditional tool of measuring shareholder value, namely, RONW revealed almost similar results., Only 28% of firm exhibited increasing trend of value addition in post-merger years. The major gainers in terms of this measure were NLC Nalco India limited, Jindal Poly Films Limited, and Jubilant Organosys Limited. were few firms that gained in post-merger years.

3) As regards to shareholder value addition in terms of markets’ assessment of it’s stoke value, 59% of firms revealed positive value in the first post-merger year. This indicated that good number of companies gained from mergers in terms of appreciation of their stoke value. However, only 17% of these firms exhibited a significant increase in the subsequent postmerger years. Twilight li-taka pharma Limited, Matrix Laborites, Hindustan Unilever Limited, Roto Pumps Limited, Rossell Tea Limited. appreciation in post-merger period. For others, stoke value gained immediately after mergers were lost in subsequent years.

B. Inter-company Analysis

1) Result of inter-firm analysis based on comparison of average values of EVA in the post-merger period revealed value erosion to the shareholders in case of 85% of sample firms. Only 15% of the firms gained shareholder value, the important achievers were Hindustan Unilever Ltd., Jubilant Organosys Ltd., and Matrix Laboratories Ltd.
2) The results of inter-firm analysis with the measure of RONW revealed almost reverse findings. As per this traditional measure, 77% of the firms gained value for their shareholders in the post-merger period indicating that mergers are profitable. Only 23% of firms were found to be non profitable. The major gainers with this measure were Pidilite Industries, ION Exchange co. limited, Dr. Reddy’s Laboratories Ltd., Gulf oil corporation Ltd., Hindustan Unilever Ltd., Hindustan Organic Chemicals Ltd.

3) With regard to market’s assessment of appreciation in shareholder value, comparison amongst firms revealed that 67% of firms gained stoke value in the post-merger period and 33% of sample firms had lost it. Few companies like Hindustan Unilever Ltd. by Shayam Telecom Ltd., NLC Nalco Limited, Bayer cropscience Ltd., Tata Infotech Ltd. (merged), Matrix Laboratories Ltd., etc.

C. Inter-industry Analysis

1) Comparison of post-merger performance of merged firms belonging to different Industry with average EVA figures revealed that in most of the industries (nine out of ten), shareholder value is lost. Only pharmaceutical industry sector gained positive value for their shareholders.

2) Similar analysis with RONW revealed almost opposite results. As per measure, merged firms in nine out of ten industries gained Trading Industries, Tea-coffee Industries, Chemicals, Petrochemicals, Electric, Electronics, Computer-hardware all have resulted in gains for shareholders in post merger period. Only merged companies in Textile industry was unprofitable.
3) Value addition in terms of markets’ appreciation of shareholder’s stake was revealed for merged firms in five out often industries with MVA as the value added metric.

D. Intra-Industry Analysis

1) M&A activity has been spread across various industry groups. Maximum number of mergers occurred in chemical and pharmaceutical industry in the last decade constituting almost 14% of our sample followed by electro, electric equipment, and electronics with nine companies in most of them. However, tea and trading industries had two to four companies falling in this sector merged.

2) Significant variations also emerged in value addition to shareholders by merged firms in these industries in terms of three value added metrics, namely, EVA, RONW and MVA. While the results revealed almost similar quantum of value addition in terms of EVA and RONW, the results for EVA and MVA were reverse. Companies in industries like electrical equipment, electronics, computer, fertilizers, textiles, packing and engineering industries, all revealed value erosion in terms of EVA and in terms of MVA.

3) The variation in quantum of value addition in terms of EVA and RONW and EVA and MVA are also corroborated by the coefficients of correlations computed between these variables for merged firms belonging to each separately. In industries like general engineering, electro electric equipment, electronics, tea, coffee, textiles, trading and engineering, correlation coefficients between new values added metric, EVA and traditional measure, RONW is very high and
significant at 1% level of significance. In case of chemical and pharmaceuticals, textiles correlation coefficients between EVA and MVA are also highly significant at 1% level of significant.

Merger Scheme Analysis

The causes or motives of mergers as elucidated in the merger schemes of fifty-six sample companies have been extensively scrutinized by tabulating them and then pattern regarding the types of merger have been traced. The findings that emerge in terms of type of merger suggests null hypothesis that mergers are not predominantly horizontal has been rejected and alternate hypothesis that mergers are predominantly horizontal has been accepted. The summarized findings are as follows.

1) An in-depth security of merger schemes revealed that the prime motives are to afford greater synergies with economies of scale, better administration, expanded capital base, better leverage, operational improvement and consequent cost savings, improve market share and achieve market dominance, achieve diversification, thus enhance growth prospects by product extension and market extension. Few mergers are undertaken for revival of sick companies and claim tax benefits in return.

2) It is further found that firms were making their efforts to consolidate in few chosen areas, thus stressing on horizontal from of mergers. A good number, almost 45% of sample firms are merger events of horizontal type, followed by mergers for revival of sick units as part of restructuring exercise
constituting 24% of the sample. These results suggest that firm prefer horizontal mergers rather than conglomerate and vertical integration.

3) Large number of mergers has also been undertaken in India at the behest of Board for Industrial and Financial Reconstruction for revival of sick companies. Most of these mergers, however, belong undertaken primarily to protect group reputation and the process, claim tax benefits available under Section 72A of Income Tax, 1961.

4) In significant number of merger cases (almost 50%), it is found that both, the merged and merging firms belonged to the same group thus indicating predominance of within-group mergers.

CONCLUSIONS AND SUGGESTIONS

The following conclusions and suggestions have been drawn from the study:

1. Mergers are not value creating strategies only. They, in fact take place for more than one objective. As is evident, from intensive security of merger schemes, the reasons include the desire and need for horizontal growth, vertical combinations, expand capital bases, get tax shelter or increase tax efficiency, correct leverage imbalances, achieve economies of scale through improvement of operations, reduced costs etc. There is, however, no body of research which suggests the relative importance of each of these motives. Several of them are generally present in each merger case.
2. Predominance of mergers seen to be either in the same product line (horizontal mergers) or within a business group (within group mergers). These patterns suggest that firm have attempted to consolidate in similar product lines. This also implies that over diversification resulting from earlier business strategies are being corrected. The regulated regime of pre-reform period often made companies within group complete with each other for market share. The economic reforms of nineties have created a liberalised environment for rectifying such mistakes.

3. Most of the mergers that took place in India during this last decade seemed to have followed the consequences of mergers of US during the same period. The results of mergers in India corroborate the conclusions of research work in US with most of the mergers not being profitable. However, most of the mergers are taking place in India to grow in size to be able to withstand international competition which they have been exposed to in the post-liberalisation regime.

4. With regard to economic efficiency and depending upon the extent of compatibility and complimentarily between merged firms, merger activities should lead to economies of scale and scope. Whether a merger is successful or not depends to what extent thee benefits are achieved. Each merger is a unique marriage and thus generalizations may not be possible. However, broadly, the result of the various analyses conducted in the study concludes that mergers have not resulted in any significant improvement in the performance of merged firms.
The fall in profitability immediately after merger may be justified by attributing this fall to various adjustment lags and rises associated with merger activities. Also, it can be hoped that after a reasonable time period when all adjustments have been made, this fall would be reversed. It does, however, raise some doubts as to the sustainability of these mergers in particular, and M&A activities in general in our economy.

6. Looking at empirical results we can say that expense ratio of the firm is significantly and negatively related to pre and post merger’s shareholders value creation. It means higher expenses lead to lower shareholder’s value which is according to the theory of finance. We also find that operating expenses of the firm is positively related to EVA and also significant at 1% level in firm’s pre and post mergers performance. ROCE of the firm is significantly also positively correlated to EVA in pre and post mergers financial performance of firm. While Debt equity, Current Ratio, and RONW are negatively correlated with shareholders creation capacity of the firm. It can be said that increase in Debt equity, Current Ratio, and RONW will leads to decrease in EVA. While evaluating the impact of acquirer of firm and scheme of merger as dummy variable are not significant. But acquirer in same group is negatively correlated with EVA.

7. In pre-merger regression analysis results shows that the value of $R^2$ is 0.86, which shows that the sample regression explain 86% of aggregate data. The overall model is also significant with adjusted $R^2$ value of 0.85. So, it can be concluded that the model applicable to Indian corporate.
Regression result of post merger indicates the value of $R^2$ and adjusted $R^2$ value are 0.87 and 0.86 which is significant at 1% level. So model is fit for study.

The classical finance theory said that firm’s shareholders value creation is based on firms earning ability and firms return on its net worth. On the basis of our regression research we have proved that the firm’s shareholders value creation is highly dependent on operating expenses, Profit market, ROCE and Expense ratio.

SUGGESTIONS FOR FUTURE RESEARCH

The area of mergers and acquisitions has been extensively researched in many developed nations especially in UK. However, not much work has been done in this area in India. The present study is a comprehensive attempt to empirically analyze the financial performance of mergers which have taken place in the year i.e. 1999-2000. But, there are some areas of research which could not be taken up in the study. It would be worthwhile for the future researchers to investigate these areas. These areas are listed below:

1. The present study has made in-depth analyses of corporate mergers in India. However, M&A activity taking place in India is not limited to corporate mergers alone as there are number of other activities like takeovers, spin offs, management buyouts, demergers etc. In fact, internationally, the term mergers and acquisitions (M&A) is now used to cover all transactions relating to the sale and purchase of subsidiaries,
divisions, brands, assets and entire company. Hence, research in this associated areas needs to be taken up.

2. The study has assessed success or failure of mergers in financial terms. Human aspect of mergers has not been touched. Gauging the success of mergers through this aspect could be another area of research.

3. Rehabilitation of sick companies by the means of merger under the aegis of BIFR has been covered as one of the motives of mergers. A studies specifically covering merger cases sanctioned by BIFR for their rehabilitation could be taken a vis-a-vis other rehabilitation schemes to find out which measures are better for revival of sick companies.

4. Long run success of mergers can be analysed by taking a longer time period, say five to seven post-merger years. For this, however, one would have to wait for few years to get the relevant data as most of the mergers in India have taken place only in past few years.

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