Chapter-2

REVIEW OF LITERATURE

This chapter provides the review of existing research work done in the area of performance evaluation of mergers and acquisition. Detailed survey of literature is done with more emphasis laid on M&A performance measurement related studies. It is an attempt to assimilate studies, observations and recommendations by earlier researchers.

This review will help to identify the research gap which will play a guiding role in setting up objectives and scope of study.

2.1 Categories of Studies on performance of Mergers & Acquisition

For the evaluation of performance of Mergers and Acquisitions existing research work can be categorized into several aspects of performance evaluation which are as follows:

1. Studies measuring performance of mergers & acquisition
2. Impact of mode of payment on the performance of mergers & acquisition
3. Impact of size of the target firm on the performance of mergers & acquisition
4. Comparison in the performance of related and unrelated mergers & acquisition
5. Impact of capital structure of acquirer on mergers & acquisition performance
6. Impact of promoter’s stake and group/non-group M&A on the post merger performance

2.2 Studies measuring performance of M&A

This Section of survey of literature has been sub-divided in the studies using the accounting, cash-flows & EVA measures for the pre & post M&A period for the evaluation of performance of mergers & acquisition and studies using the event study methodology around the announcement of mergers & acquisition.
2.2.1 Studies using the accounting, cash-flows & EVA measures:

Hogarty (1970) attempted to pinpoint some of the sources of the conflicting findings in the analysis of M&A performance. This is done by comparing the investment performance and earnings per share growth of active acquirer to that of their respective industries. The first finding of this investigation was that the investment performance of heavily merging firms was generally worse than the average investment performance of firms in their respective industries. Second, all the measures used resulted in "success distribution" this exhibited high relative variability. The stock price performance of active acquirers was worse than their earnings per share performance; it implied that mergers are a risky form of investment. While most active acquirer did not obtain an attractive return, a few did. The relatively few successful acquirers obtained very large returns. The prospect of these large returns tempted the other firms to engage in merger activity.

Neely and Rochester (1982) analyzed the risk characteristics, profitability and performance benefits attained by merging savings and loan associations (S&Ls). A sample of associations merged in 1976 was matched with a group of non-merged associations. Data for up to five semi-annual periods after merger were examined for differences between the two groups in the periods coincident with and after the merger. Differences in ratios intended to measure income/profitability, expense/efficiency, asset structure, and risk/asset quality were analyzed. The two groups were also analyzed through multivariate procedures by employing Multiple Discriminant Analysis (MDA) in order to determine if additional variables, in combination, contribute more information and are more powerful than the univariate tests in distinguishing between the two groups.

This study has provided the evidence that significant differences do exist in key financial measures between merging and non-merging S&Ls in US. Yet evidence of synergy as measured by increased profitability of merging associations in net income to assets, could not be verified. Only weak evidence of synergy, as measured by return on net-worth, was proved for merging associations. Acquiring S&Ls operating performance improved from the merger period throughout the post-merger period, particularly with respect to gross operating income.
Lubatkin (1983) in his paper has reported an in-depth review of the findings of studies that have investigated either directly or indirectly the question, "Do mergers provide real benefits to the acquiring firm?" Literature primarily from the field of industrial organizations suggested that acquiring firms may benefit from merging because of technical, pecuniary, and diversification synergies. Empirical studies, however, almost exclusively in the field of finance and using a performance measure recently developed from the capital asset pricing model, found that all the significant gains of merger go to the acquired firms. A problem with these studies was that they treat merger as a homogeneous phenomenon. Strategic management literature recognized that mergers are not a homogeneous phenomenon. Rather, they can lead to a range of possible outcomes contingent on the strategic fit between acquired and acquiring firm.

Ravenscraft and Scherer (1989) tested the hypothesis that other variables maintained equal, if mergers result in economies of scale or scope, the post-merger profits should be higher than the pre-merger profits and/or their industry averages. Their study of 2,732 lines of business for the years 1975-77 did not find any improvement in the post-merger operating performance. In fact, with no control for the merger accounting methods (purchase vs pooling), there was a significant negative impact of 13.34 per cent on the post-merger profitability. One important shortcoming of the Ravenscraft and Scherer study was the non-alignment of the post-acquisition period with the acquisition event, leading to non-validity of the results.

Healy, Palepu and Ruback (1992) addressed the issue of whether mergers improved performance, and if they did so, what the sources of economic gain were. They stated that traditional stock price performance studies have been unable to determine whether mergers lead to long-term economic gains, resulting in a gap in our understanding of post-merger firm performance. They addressed this gap through this research work. They also tried to improve upon the methodology of the earlier work by Ravenscraft and Scherer (1989). A sample of the 50 largest mergers of public industrial firms in the U.S. completed between 1979 and mid-1984, was used. Cash flow measures were used to study the post-merger performance. According to them, cash flows are representative of the actual economic benefits generated by the assets. Pre-tax operating cash flow returns on assets were used to measure the improvements.
in operating performance. Their definition of operating cash flow was sales, minus cost of goods sold and selling and administrative expenses, plus depreciation and goodwill expenses. This measure was deflated by the market value of assets (market value of equity plus book value of net debt) to make it comparable across time and firms. This measure was unaffected by depreciation, goodwill, interest expense and income, and taxes. The aggregate industry-adjusted pre-merger and post-merger performance measures were calculated, five years prior to and subsequent to the merger, and then these two were compared to study the change in post-merger performance. The firm-specific, economy, and industry factors that might influence post-merger performance, were thus controlled for. An increase in the post-merger operating cash flow returns vis-à-vis the firms' industries was observed. The increase was 2.8 per cent per year, after controlling for the pre-merger performance. The improvements in operating cash flows after merger were due to enhancement of asset productivity post-merger. Healy, Palepu and Ruback also correlated their post-merger cash flow performance and merger-announcement related stock market performance and found a significant positive correlation between these two measures indicating that the stock market correctly revalues the merging firms at announcement in expectation of the improvements in operating performance in the future.

Cornett and Tehranian (1992) studied the post-acquisition performance of 30 large banks in the United States. These acquisitions took place between 1982 and 1987. Each of these acquisitions had a purchase price exceeding $100 million. They measured economic performance related to the mergers in a manner similar to Healy, Palepu and Ruback (1992). Operating cash flows divided by the market value of assets were used for performance evaluation. The pre-merger performance was computed for years -1 to -3 before the merger, whereas post-merger performance was studied over the years +1 to +3 after the merger. Comparing the latter with the former is indicative of the impact of the merger on firm performance. The industry mean data was subtracted from the raw sample-firm data to provide the industry-adjusted performance, prior to the comparison between the pre and post-merger figures. This was done to ensure that the influence of economy-wide or industry factors on the performance data calculated was avoided. There was a significant (at the 1% level) increase of 1.2 per cent in performance post-merger as compared to before the
merger. This study pertained specifically to the US banking industry and hence its results may not be generalizable across other industries. Also, like in the Healy, Palepu and Ruback's (1992) paper, selecting only the largest mergers may lead to results that cannot be generalized across all sizes of mergers, such as the ones taking place in India. Nevertheless, the methodology adopted here serves as a guiding post for future studies of the same kind.

Switzer (1996) used the methodology followed by Healy, Palepu and Ruback (1992), focused on analyzing the post-merger changes in operating performance. Researcher’s contention was that the latter study covered the "merger mania" period in the US and not mergers in general. It thus made sense, according to Switzer, to take up a longer period of mergers in the US, in order to be certain about the applicability of the results of such a study to periods not witness to a merger wave. The study was of 324 acquisitions occurring between 1967 and 1987 in the US, using the cash flow-based measure of operating performance as in Healy, Palepu and Rubach (1992). It concluded that mergers led to synergistic gains and better performance in the long-term, the median improvement over five years post-merger being a significant 1.97 per cent.

Larsson and Finkelstein (1999) followed an approach that differed from traditional methods of studying mergers and acquisitions in three ways (1) the success of a merger or acquisition was gauged by the degree of synergy realization rather than more removed and potentially ambiguous criteria such as accounting or market returns; (2) the key attribute of combination potential was conceptualized not only in terms of the similarities present across businesses, as in most studies of mergers and acquisitions, but also in terms of the production and marketing complementarities between the two businesses; and (3) the data were derived from a case survey method that combined the richness of in-depth case studies with the breadth and generalizability of large-sample empirical investigations. The framework was tested empirically across a sample of 61 mergers and acquisitions. The extent to which a merger or acquisition resulted in synergistic benefits was related to the strategic potential of the combination, the degree of organizational integration after the deal
was completed, and the lack of employee resistance to the integration of the joining firms.

Manson et al. (2000) studied 44 takeovers in the UK completed between January 1, 1985 and December 31, 1987, wherein the total market value of each of the acquired firms was over £5 million, in a re-examination of the issue of whether UK takeovers resulted in operating gains for the merging firms. They used the cash-flow based measure of operating performance as also the research methodology innovated and introduced by Healy, Palepu and Ruback (1992) and Cornett and Tehranian (1992). Regressing post-takeover operating performance on pre-takeover operating performance using eight variants of the measure, they found that takeovers had led to operating gains ranging from 2 per cent to 14 per cent per year postmerger. This study also provided evidence for non-operating gains resulting from takeovers.

Ghosh (2001) focused on merging firms’ operating performance after corporate acquisitions. The sample consisted of 315 pairs of target and acquiring firms for which mergers were completed between 1981 and 1995. The performance measure used was operating cash flows, both pre- and post-merger, defined as sales minus cost of goods sold, minus selling and administrative expenses, plus depreciation and goodwill amortization expenses. The study compared the pre- and post-acquisition performance of merging firms using control firms as benchmarks, instead of using industry-median benchmarks as used in Healy, Palepu and Ruback (1992). Ghosh contended that using industry-median benchmarks could lead to non-random measurement errors since firms undertake acquisitions following a period of superior performance. The control firms were matched on the basis of similar operating cash flow performance and total asset size before the acquisition. Both size and preacquisition performance were thus accounted for. Using a methodology similar to Healy, Palepu and Ruback (1992), the study found that the cash flows of merging firms increased significantly by 2.4 per cent every year. The median increase in cash flows post-merger by 0.26 per cent per year was statistically insignificant, when the sample firms were compared with matched firms. This paper assumed that only large-sized and well-performing firms generally go in for mergers. This assumption may
not be valid in the Indian M&A context where we have even small and underperforming firms adopting the merger route to growth and to satisfy other motives.

Sharma and Ho (2002) investigated whether corporate acquisitions create synergies reflected in corporate operating performance measures. They analyzed a sample of 36 Australian acquisitions occurred between 1986 to 1991 using matched firms to control for industry and economy-wide factors. The study found that on the basis of four accrual and four cash flow performance measures, corporate acquisitions did not lead to significant post-acquisition improvements in corporate operating performance. The results were consistent with Casey et al.'s (1987) Australian capital markets study. The various performance indicators employed in this study explained that inconsistencies in prior research could be attributed to differences in performance indicators used to capture synergistic benefits. The study also found that the type of acquisition (conglomerate versus non-conglomerate) and the form of acquisition financing (cash, share or a combination) do not significantly influence post-acquisition performance. Similarly, the size of the acquisition and the payment of a premium (goodwill) do not influence post-acquisition performance. While the results were not consistent with the synergy theory underlying corporate acquisitions, the results were interpreted consistent with the agency, the hubris and the financial motivation hypotheses. This was consistent with the arguments of Bujega and Walter (1995). Specifically, Bujega and Walter (1995) concluded that management of Australian acquirers tend to elevate their interests to the detriment of the shareholders'. This suggests that corporate acquisitions in Australia may not be undertaken for synergistic reasons.

Agrawal and Jaffe (2003) examined the issue of underperformance of takeover targets in a large scale empirical study and with a number of methodological improvements. First, they examined both operating and stock return performance prior to acquisition. Second, they measured operating performance after adjusting for size, industry, and past performance, as suggested by Barber and Lyon (1996). Third, they calculated long-term abnormal stock returns for the 1965-1996 period, after adjusting for firm size, book-to-market, and momentum. In addition, based on the findings of Lyon, Barber, and Tsai (1999), their analysis used equally-weighted portfolios of monthly
abnormal returns and avoided the new listing bias in forming control portfolios. They computed f-statistics using the calendar time abnormal returns (CTAR) methodology. Fourth, they proposed an improvement on the calendar portfolio method of Jaffe (1974) and Mandelker (1974). Fifth, they used a large sample of acquisitions spanning a 71-year time period and examined performance over 100 months before the acquisition announcement. Sixth, they performed a rigorous examination of subsamples where takeovers were more likely to be disciplinary.

Whether analysing operating or stock returns, they found no evidence of pre-acquisition underperformance for the target sample as a whole. The test statistics were insignificant over virtually all the intervals they examined prior to the acquisition announcement. In addition, pre-acquisition performance was economically small. The median values of OPA and OPS were actually greater for targets than for controls in most of the pre-acquisition years that they examined. For stock returns, the CAAR from month -100 to month -3 for the entire 1926-1996 period was only -1.93%. The results here are consistent with the previous literature where there is little evidence of pre-acquisition underperformance for the entire sample of targets.

Ramaswamy and Waegelein (2003) studied the post-merger financial performance of 162 merging firms that occurred during 1975-1990 in the US. They used industry-adjusted operating cash flow returns on market value of assets as the measure of performance, which was similar to the one used by Healy, Palepu and Ruback (1992). Even their methodology was the same as in the latter, except that they used only firms that had not gone in for any merger during the study period as part of their control sample, since they felt that only that would make the data incorruptible and the results more robust. They examined the financial performance of the combined target and acquiring firms over a period of 5 years post-merger period in relation to the corresponding pre-merger period. The study found a significant increase in firm performance after the merger had taken place. The study found that the post-merger performance was negatively associated with the relative target size and positively associated with long-term incentive compensation plans. Firms that were in dissimilar industries also showed improved performance.
Rahman and Limmaek (2004) tested for evidence of operating improvements in Malaysian acquisitions by examining operating performance for a sample of 94 quoted acquiring and 113 target Malaysian companies involved in acquisitions over the period January 1, 1988 to December 31, 1992. The majority of target companies that were included in the sample were private companies and were therefore much more likely to be entering into voluntary combinations with their acquirer than is often the case in other studies. Therefore they did not expect to observe the same characteristics in their sample as those that were hypothesised for companies involved in disciplinary takeovers.

The initial analysis confirmed this view as, prior to the acquisition, target companies had higher operating performance than their control companies, but acquiring firms have lower operating performance than either their controls or the target companies. The results of subsequent analysis suggested that operating cash flow performance for combined firms in Malaysian acquisitions improved significantly following acquisitions.

Analysis of the components of operating cash flow indicated that improvements in post-acquisition performance were driven both by an increase in asset productivity and also by the higher levels of operating cash flow generated per unit of sales. Increases in capital expenditure rates in the post-acquisition period suggest that the combined firms have not sacrificed their long-term investments for the sake of short-term profitability.

The findings of this paper raised several interesting issues for future research. The conclusion that acquisitions improve post-acquisition operating performance, based on analysis of operating cash flows, appears to be contrary to the results reported in those studies in the UK and the US that have employed accounting data to examine improvements in operating performance. A pattern of negative post-acquisition performance reported in accounting-based studies may be a consequence of the acquisition accounting methods adopted or potential earnings manipulation, neither of which affected the measurement rules used in this study. The results, however, suggested that at least in Malaysian acquisitions, there is the potential for improvements in operating performance. The results also suggested that opportunities
for economic gains from takeover activity may also differ according to the form and
ownership characteristics of targets.

Yook (2004) examined post-acquisition performance of acquiring firms using EVA. He stated that whereas examining long-term stock returns has been a popularly used approach, the use of accounting and financial data is appropriate to measure directly post-acquisition operating performance gains. Traditional accounting rate of returns and profitability measures are criticized for their deficiencies in measuring performance, particularly because they ignore capital costs and have the potential for manipulation of accounting data. A new performance measure, EVA, overcomes these flaws existing in conventional financial metrics as a true performance measure.

After examining 75 large acquisitions occurring during 1989 to 1993, this study found that acquiring firms experienced significantly deteriorating operating performance after the completion of acquisitions. The results indicated that the sharp decline in the raw EVA was mostly accounted for by the industry effects. This reinforced the view that industries experiencing relatively poor operating performance are likely to be the object of takeover activity.

A different picture unfolded when premiums paid to target firms were taken into account in the analysis. When EVA was calculated assuming that no premium was paid to target firms, i.e., the premium was excluded from the acquiring firm’s capital in the post-acquisition period, industry-adjusted EVA showed a slight improvement. The post-acquisition aggregate median EVA for this sample increased $5 million compared to the pre-acquisition period. These results suggest that acquiring firms tend to experience slightly improved performance relative to their industry counterparts after completion of the acquisition. But the improved operating performance is negated by the capital costs of the large premiums paid to the target firm, creating no real economic gains to the acquiring firm’s shareholders. These findings indicate that acquisitions are zero net present value investments for acquiring firms.

In addition, this study examined whether post-acquisition performance differs across the transaction characteristics that include type of acquisition (mergers or tender offers), method of payment (cash or stock), business similarity between the acquiring
firm and the target firm, and premiums paid to target firms. Among these four characteristics only the mergers/tender offers variable is statistically significant. The findings indicate that larger premiums paid in tender offers can be justified by the higher improvement in operating performance later.

Gregory (2005) used a dataset of UK take-overs and proxies for free cash flow similar to those used by Lang, Stulz and Walking (1991), they found no support for the FCF hypothesis and showed that this conclusion was robust to the model of long run returns employed. Contrary to the free cash flow hypothesis there was evidence that acquirers with high free cash flow performed better than acquirers with low free cash flow. Although not consistent with the Jensen hypothesis, this evidence was compatible with the emerging UK evidence that shows cash flow-to-price measures are associated with market returns.

Cornett, McNutt and Tehranian (2006) examined bank performance around mergers. While previous research has examined the performance of banks around a merger, changes in long-term operating performance (including an extensive examination of the revenue enhancement and cost reduction sources for any performance changes), for both large and small bank mergers were not examined. This paper filled this void. Further, the paper examined performance changes before and after the passage of the Riegle-Neal Act. The empirical results led to the conclusion that industry-adjusted operating performance of merged banks increased significantly after a merger. They also found that large bank mergers produced greater performance gains than small bank mergers, activity focusing mergers produce greater performance gains than activity diversifying mergers, geographically focusing mergers produce greater performance gains than geographically diversifying mergers, and performance gains were larger after the implementation of full nationwide banking in 1997 via the Riegle-Neal Act. Further, they found the improved performance was the result of both revenue enhancement and cost reduction activities. Additionally, the revenue enhancement opportunities appeared to be more profitable in those mergers that offered the greatest opportunity for cost cutting activities, i.e., activity focusing and geographically focusing mergers. Finally, they found that along with the increase in
accounting-based operating performance. The merged banks also experienced positive abnormal long-run stock returns.

Homburg and Bucerius (2006) stated that previous research on mergers and acquisitions has neglected the issue of speed of post-merger integration by and large. This paper argued that there are benefits and detriments associated with speed of integration. Thus, in some situations speed may be highly beneficial whereas in others it may be harmful to the success of a merger or acquisition. Results from a survey of 232 horizontal mergers and acquisitions showed that speed is most beneficial when external relatedness is low and at the same time internal relatedness is high. In contrast, speed is highly detrimental in the case of low internal and high external relatedness.

Cloodt, Hagedoorn and Kranenburg (2006) examined the post-M&A innovative performance of acquiring firms in four major high-tech sectors. Non-technological M&As appeared to have a negative impact on the acquiring firm’s post-M&A innovative performance. With respect to technological M&As, a large relative size of the acquired knowledge base reduced the innovative performance of the acquiring firm. The absolute size of the acquired knowledge base only had a positive effect during the first couple of years after which the effect turns around and a negative effect on the innovative performance of the acquiring firm was visible. The relatedness between the acquired and acquiring firms’ knowledge bases had a curvilinear impact on the acquiring firm’s innovative performance. This indicated that companies should target M&A ‘partners’ that are neither too unrelated nor too similar in terms of their knowledge base.

Liu, Chen and Pai (2007) investigated the difference in corporate performance evaluation between telecommunications companies that did and did not pursue M&A strategies. It also discussed the corporate performance of specific companies before and after M&A transactions. Data envelopment analysis was applied to assess the performance of 60 Taiwanese telecommunications companies, based on 20 financial indicators. The empirical results revealed that M&A strategy does not seem to enhance corporate performance in the telecommunications industry, whilst an internal growth strategy does improve corporate performance.
Mcnamara, Halebian and Dykes (2008) assessed industry acquisition waves from 1984 through 2004. Acquisitions often occur in waves within industries. They extended the theoretical understanding of such waves by drawing upon research on early mover advantage and bandwagon effects to develop arguments regarding the likely performance potential of participating at different points in an acquisition wave. In line with their theoretical model, they found acquisition performance was higher for early movers but lower for acquirers that participated at the height of the acquisition wave. Although they found this general performance trend, their findings suggest both industry and acquirer characteristics influence the degree to which firms seize early mover advantages or fall prey to bandwagon pressures.

Ullah, Farooq, Ullah and Ahmad (2010) examined whether corporate marriages (M&A) long lasting and productive in term of value? They have analyzed the pre and post-merger performance of Glaxo Smith Kline by applying the net present value approach of valuation. Company has substantially reduced the cost $1.8 a year, to be comprised of combining their R&D operations, manufacturing consolidation and substantial headcount reduction. Any how the debate of value creation in future is still questionable.

Abd-Kadir, Selamat and Idros (2010) investigated the extent of merger and acquisition activity affect Malaysian banks' productivity over the period 2003-2007. It analyzed both the technological changes and also technical efficiency changes of the merged banks in Malaysia using a nonparametric Data Envelopment Analysis (DEA) and Malmquist Index approach. It was found that total factor productivity (TFP) had increased in six out of the nine banks tested with the mean total TFP for all banks also recorded an increase of 10.1%. This increase was attributed solely to technological advances, such as innovations in the banking technology. Moreover, this study revealed that the process of mergers and acquisitions has actually increased the efficiency and productivity growth of the banking groups in Malaysia.

Ismail, Abdou and Annis (2011) examined the operating performance of a sample of Egyptian companies involved in Mergers and Acquisitions (M&A) transactions for the period 1996 to 2003. The analysis was based on the accounting measures to test
the effects of M&A on the corporate performance of the construction and technology sectors.

Total sample analysis indicated that M&A did not affect the operating performance of the Egyptian merged companies. With respect to sector level, the findings suggested that M&A in the construction sector has contributed in improving firms' profitability but failed to improve efficiency, liquidity, solvency and cash flow position, whereas in the technology sector it has not. The results might be explained and justified based on the following first, the industry sector has an effect on the success of M&A. By analyzing the financial statements of both the sectors, reports of the board of directors, and information published in Kompass Egypt Financial Year Book, it can be concluded that none of the two sectors encountered different circumstances internally or externally other than M&A transactions. Therefore, differences in performance resulting in the two sectors relate mostly to the type of sector.

Lahovnik & Malenkovic (2011) examined the factors that influenced the performance of acquisitions in Slovenia. The performance of an acquisition was measured by comparing the acquisition's motives with its outcomes. The acquisitions were divided into three types: horizontal, vertical, and conglomerate. The research sample included 31 horizontal acquisitions, 23 conglomerate acquisitions, and 4 vertical acquisitions for the period 1998-2008. Managers who answered the questionnaires had been included from the start of the acquisition process and were well aware of all strategic factors that determined the acquisition. The result of this research implicated that the so-called strategic and organizational fit between companies involved in M&A play an important role in improving the operational performance of the acquired companies in the post-acquisition period. Increasing relatedness—especially with regard to certain competencies and skills—between companies involved in an acquisition increases the chances of success.

Hao and Howe (2011) examined the effects of the two types of merger structures from the shareholder point of view. Where two structures are one-step and two-step transactions. In order to compare the shareholder wealth effects of merger structure, the authors control for deal and firm characteristics and the endogenous nature of the choice of transaction form. Specifically, the authors follow the literature to use a
switching regression framework with endogenous switching to address endogeneity. No evidence was found of detrimental effects of two-step mergers on target shareholders. The findings suggested that at least some one-step mergers could benefit from using the two-step structure. The authors provided several explanations for the continued use of one-step mergers.

Sood and Kaur (2004) analyzed the post-takeover performance of the target firms. The study utilized a sample of 20 companies targeted during the financial year 1997-98. The mean value of a set of eight financial ratios based on a period of three years each immediately preceding and succeeding the takeover attempt were calculated and compared. The two profitability ratios viz. EBIT/Sales and ROCE indicated a significant decline in the performance of target companies in the post-takeover period. This was reinforced by the fact that their efficiency, as measured by Asset Turnover ratio also declined substantially. Also the liquidity and solvency position of these companies, as shown by current ratio, cash flow to sales and debt-equity ratio, have not shown any significant improvement. Further the market response to these takeovers as indicated by FV/EV and market price to book value also presented a dismal picture. None of these ratios was found to be significantly different in the two periods when tested in terms of t-test. In sum, the results reported indicated that post-takeover performance of the target firms have, in general, deteriorated on different parameters.

Kumar and Rajib (2007) examined the post-merger operating performance of merged firms. The analysis in this study was based on the 57 large mergers that occurred during 8-year period between 1995 and 2002. To be included in their sample, a firm had to meet the following conditions. First, it acquired a firm whose asset size constituted at least 10% of its own asset size. The asset size for both firms were measured at the beginning of the year in which merger took place. The first condition was imposed to concentrate on large mergers. Second, the acquiring firm's financial data were available for a period of three years before and after the year of merger. Third, those mergers were eliminated from the sample if the acquirer firm was involved in more than four mergers over the event period in order to reduce the problem of confounding events. For each of the acquiring firm and target firm, a
matched control firm was selected from the same industry and asset size group. The pre and post-acquisition operating cash flow performance of merging firms relative to matched firms were compared to determine whether operating performance improved following mergers. Merging firms were matched on the basis of pre-acquisition performance and size. Three alternate methodologies were utilized for the study in which cash flow was deflated by market value of assets, book value of assets and the sales value. The results based on book value of assets and sales model provide some evidence to suggest that corporate performance improved after mergers. The model based on market value of assets doesn’t support the hypothesis that operating performance improves after mergers. The use of different deflators - accounting measures versus market measures which were sensitive to market revaluations have contributed to different results.

Mantravadi and Reddy (2007) studied the impact of mergers on the operating performance of acquiring corporates in different industries, by examining some pre-merger and post-merger financial ratios, with the sample of firms chosen as all mergers involving public limited and traded companies in India between 1991 and 2003. The pre-merger and post-merger averages for a set of key financial ratios were computed for 3 years prior to, and 3 years after, the year of merger completion. For the years prior to a merger, the operating ratios of the acquiring firm alone were considered. Post the merger, the operating ratios for the combined firm were taken. The post-merger performance was compared with the pre-merger performance and tested for significant differences, using paired “t” test. Only mergers where equity stock of acquiring firm was issued to acquired firm (target) shareholders, as consideration for the acquisition / merger have been considered for the study. Instances where there have been only cash acquisitions were excluded from this study, to ensure comparability of results across the sample. Also deleted from the list were mergers where the relative size was less than 10%, as it was felt that such low-size acquisition cannot make a significant impact on operating performance of the acquiring company. The results suggested that there are minor variations in terms of impact on operating performance following mergers, in different industries in India. In particular, mergers seem to have had a slightly positive impact on profitability of firms in the banking and finance industry, the pharmaceuticals, textiles and electrical
equipment sectors saw a marginal negative impact on operating performance (in terms of profitability and returns on investment). For the Chemicals and Agri-products sectors, mergers had caused a significant decline, both in terms of profitability margins and returns on investment and assets.

Ramakrishnan (2008) tested the hypothesis that mergers in India have helped firms perform better in the long-term. He initially identified 414 mergers between 1993 and 2005. Mergers taking place in the financial sector were dropped due to differing accounting standards applicable to them that make comparison with other firms difficult. Only domestic mergers taking place in India were selected. Cross-border mergers, i.e., in which either the bidder or the target was based outside India, were dropped.

The final sample size used for analyses was thus 87 pairs of mergers consisting of 174 firms (87 each of targets and bidders). The average relative size of the target to the bidder firm was 0.59, where size was measured as the total assets of the firm. He applied paired t-test on 3 years pre and post merger industry adjusted performance measure, CFFO. He also applied regression analysis to filter out the impact of pre-merger performance on post-merger performance.

He concluded that, on an average, merging firms in India appear to have performed better financially after the merger, as compared to their performance in the pre-merger period. This improvement in performance can be attributed to the merger. Synergistic benefits appear to have accrued to the merged entities due to the transformation of the uncompetitive, fragmented nature of Indian firms before merger, into consolidated and operationally more viable business units. What this study thus indicates is that in the long run, mergers appear to have been financially beneficial for firms in Indian industry.

On studying the long-term post-merger performance of firms by the two constituents of the measure of performance (operating cash flow scaled by the assets) – operating margin and sales turnover – this study obtained some insights into the sources of economic gains. The long-term post-merger operating margin of firms, on an average, appears to have improved. This means that higher incremental operating cash flows
are being generated per unit net sales by the firms after the merger. This means that higher profits (before accounting for depreciation, interest, and taxes) being generated through the net sales. This might also indicate size effects, i.e., the economies of scale obtained by the merged firms due to which the fixed costs appear to have been lowered. On the other hand, there does not appear to be any change in the sales turnover of the firms, on an average, after the merger. Therefore, it cannot be concluded that the net sales per unit of asset invested have increased after the merger, i.e., the increase in the efficiency of utilization of assets to generate higher net sales cannot be inferred from these findings. To sum up, this study renews or reaffirms confidence in the Indian managerial fraternity to adopt M&As as fruitful instruments of corporate strategy for growth.

Singh and Mogla (2008) studied a sample of 56 companies merged between 1994 and 2002 and compared the pre-merger and post-merger operating performance of merged companies. The analysis was done by calculating the mean performance values as well as the significance of their differences using the t-test across the pre-merger and post-merger periods. Besides, regression analysis was applied to find the significant variables affecting the profitability. Regression results indicated that profitability declined significantly after the merger. Current ratio, debt equity ratio and size bear a negative impact on profitability. Interest coverage ratio contributes positively towards profitability. Group firms were likely to show improved performance in future.

The study highlighted that even after five years of merger, the firms could not improve their performance. Similar decline in performance was observed for matching firms. Thus, the decline in the performance of merging firms cannot be attributed to merger alone, rather it seems to be economy specific. It was found that there were strong prospects of improvements in profitability. Group and unrelated firms may improve when compared to non-group and related firms in terms of RONW, while ROCE would improve in related and group firms. Interest coverage is a better predictor of profitability than debt-equity ratio. Overall, it can be said that with the passage of time, the profitability of merged firms would improve as indicated by the significantly positive coefficients of constant and age.
Mann and Kohli (2005) empirically evaluated the synergistic gains from bank mergers by dividing them into two categories of forced mergers and market driven mergers. In order to evaluate the market reaction towards the announcement of bank mergers, firstly, the standard event study methodology as pronounced by Fama (1976) and Fama and MacBeth (1973) has been applied. Thereafter the paired sample technique has been applied to measure the post-merger financial performance of these banks to find out whether the market has correctly assessed the worth of the merger at the time of its announcement or not.

The empirical results indicate that markets have reacted negatively to the announcement of forced mergers while the reaction has been positive to that of market driven mergers. In line with the market expectation, forced mergers have not added any value to both the balance sheet and profitability variables of merged banks in the post-merger period. Although market driven mergers have not immediately improved the profitability of merged banks, but they have improved the balance sheet variables of merging banks and have provided these banks an edge over the competitors in terms of geographic dispersion, influence in new regions where the merging entity lacked presence and extended product portfolios and thus have provided a better vehicle for growth.

Singh (2009) analyzed the recent mergers (involving both private and nationalized banks) by using the Data Envelopment Analysis (DEA). They analyzed 10 mergers of reasonable size in the post-2000 period. They analyzed the profit efficiency and cost efficiency of the acquiring bank to see whether there have been gains from consolidation. They found that while mergers don't seem to impact the cost and profit efficiency in an adverse manner and whatever loss that happened initially was recovered quickly. The private sector mergers that have taken place since the turn of the millennium have shown positive results. In case of PSBs there has been no market driven merger. They maintained that they do not have sufficient evidence to accept or reject any of the efficiency hypothesis in case of PSBs.

Sinha and Kaushik (2010) examined the impact of mergers and acquisitions on the financial efficiency of the selected financial institutions in India. The analysis consisted of two stages. Firstly, by using the ratio analysis approach, they calculated
the change in the position of the companies during the period 2000-2008. Secondly, they examined changes in the efficiency of the companies during the three years pre and post-merger periods by using nonparametric Wilcoxon signed rank test. This study concentrated on the financial sector companies. The sample under study included 17 companies in financial sector.

Overall, the result of the study indicated that in most of the M&A cases, in the long run the acquiring firms were able to generate value creation in one or the other form, that is higher cash flows because of cost cutting and greater market power, however in spite of improved financial performance sixty four per cent of cases showed increased debt to equity ratio. Profit before tax in all the merging cases has shown a positive trend for financial sector companies.

Singh and Mogla (2010) examined the profitability of acquiring firms in the pre- and post-merger periods. The sample consisted of 153 listed merged companies. Five alternative measures of profitability were employed to study the impact of mergers on the profitability of acquiring firms. The results reveal that profitability declined in 55% of companies, and only 29% of companies could improve their profitability. Profitability results were not robust to the various measures applied in the study. For a few companies, though OPM, NPM, and ROCE declined, their RONW improved. ROCE, which is called master ratio, seemed a better measure of profitability than RONW. Out of the total 153 acquirers, 38 companies acquired sick units, and the remaining 115 acquired healthy units. Profitability analysis was conducted for these two groups. Around 55% of the companies experienced a decline in profitability in both the groups. DuPont analysis revealed that ATR declined significantly, whereas OPM improved significantly following the merger. Therefore, profitability declined due to poor asset utilization. Irrespective of the fact whether the acquired units were healthy or loss-incurring, profitability of acquirers remained the same in both the cases. It suggests that managers should give due attention to proper utilization of newly acquired assets.

Ramakrishnan (2010) analyzed the performance of merged companies and factor influencing it. Pre-tax operating cash flow deflated by the operating assets was used to measure firm Performance The raw firm operating performance figures calculated
were adjusted for industry and economic effects. The change in performance on account of the merger was captured by comparing the post and pre-merger performance measure. A paired-samples t-test was carried out to evaluate whether the difference between AIACFI.POST and AIACFI.PRE was statistically significant. He concluded that mergers have enhanced the long-term performance of firms in India. This improvement was on account of higher efficiency of utilization of assets.

Unrelated mergers appeared to be performing better in the long term, contrary to strategic management theory. However, due to a majority of the unrelated firms in the sample belonging to the same business groups the result may be indicative of other benefits of such mergers leading to better results. This needs to be probed in future research. The relative size of the acquired firm and the method of payment did not seem to be playing a significant role in influencing post-merger returns.

The studies based on pre and post merger analysis of accounting measures have shown mixed results. On the other hand, studies which have used cash flow measures have shown the improvement in the performance as a result of merger.

2.2.2 Studies using Event Study Methodology

Clark and Ofek (1994) tested the effectiveness of restructuring of failing firms by mergers. They collected a sample of 38 takeovers occurring between 1981 and 1988 that were attempts to restructure distressed targets. They used five measures of post-merger performance to examine the ability of an acquirer to successfully revitalize a target that is experiencing operating or financial difficulties. Bidders had negative post-merger performance using all five measures. Much of the post-merger decline appeared to be caused by industry factors. While their results indicated that bidders’ shareholders lose, they could not conclude that mergers are a poor choice for restructuring a distressed target.

Abnormal announcement period return on the bidder’s shares was positively and significantly related to the post-merger return earned by bidders on their investments in the targets. They studied the influence of various factors in post-merger performance. Bidder overpayment helped to explain poor restructuring performance. Distressed targets that were smaller relative to bidder were associated with
restructuring efforts that yield positive returns to the bidder. Target firms that were financially distressed prior to the takeover were more likely to be successfully restructured. Higher levels of post-merger leverage for the combined firm were associated with worst merger performance. Buyers of distressed firms seldom got concession but concession increased the post-merger performance.

Tsung-Ming and Hoshino (2000) attempted to find out whether value was created in Taiwanese mergers through tapping of economies of scale. Their sample consisted of 20 firms that acquired other firms between 1987 and 1992. Both stock market-based and accounting-based measures were used to assess shareholder wealth gains and improvements in corporate performance post-merger. Accounting measures were used to determine the profitability, financial health, and growth of the acquirers post-merger. Industry medians were computed for each year corresponding to the merging firms. The industry median pertained to all the publicly-listed firms of the same industry as per the sample and year. These control firm values/industry medians were then subtracted from the pre- and post-merger values obtained for each firm. These pre- and post-acquisition adjusted values were compared to arrive at the performance of the merged firm. They found no profitability improvements post-merger for the acquirers. In fact, there was deterioration in some profitability indicators. There was no significant difference in the pre- and post-merger values for leverage and debt equity while the current ratio fell significantly in the first year after the merger while not being significantly different in the later years. They calculated sales growth as \(\frac{{\text{sales of current year}}}{\text{sales of previous year}} - 1\). The acquirers significantly underperformed on this measure post-merger. The study had taken into account only the acquiring company. Most of the targets were privately-owned companies. In most cases, the merger was a result of government intervention since the healthy acquirer was forced into taking over the distressed and financially weak acquired firm. This might have led to the deterioration in the condition of the acquiring firm leading to a downturn in profitability post-merger. The results of this study are hence not generalizable.

Baesel and Grant (2001) examined the risk-adjusted performance of a sample of Canadian firms actively involved in acquisition programmes. There was a wide
variety of types like horizontal, vertical and diversifying and of motivations like defensive and diversified. As per them, within the limits of their sample they concluded

- Acquisition oriented firms performed in a manner similar to a control group of non-acquisition oriented firms. The performance of the control and acquisition sample was approximately the same in both the good market period, 1960-69, and the poor market years, 1970-75.
- Both the control group and the acquisition oriented firms performed at least as well and possibly better than the market index. The performance of both the control sample and the acquisition sample was significantly better than the market index in the good market period, 1960-69, and approximately the same as the market in the poor market period, 1970-75. For the entire period, 1960-75, both the acquisition sample and the control group out-performed the market, and the mutual funds, but did not exhibit statistically significant difference in performance from each other.

DeLong (2003) stated that there is a paradox in bank mergers. On average, bank mergers do not create value, yet they continue to occur. Using cross-sectional analysis to examine 54 bank mergers announced between 1991 and 1995, the researcher tested several facets of focus and diversification. Upon announcement, the market rewards the mergers of partners that focus their geography and activities and earnings streams. As per the results of this study, only one of these facets, focusing earnings streams, enhances long-term performance. Two other circumstances improve long-term performance 1) When a merger involves a relatively inefficient acquirer and 2) When partners reduce bankruptcy costs.

Jakobsen and Voetmann (2003) investigated the short-run price adjustment around acquisition announcements and the long-run upward bias of cross-sectional average buy-and-hold returns. The geometric Brownian motion model was applied to decompose the cross-sectional average long-run returns into transformed mean and volatility components. The decomposition improved the interpretation of security performance. The methodology was demonstrated on the security performance of bidding firms listed on the Copenhagen Stock Exchange. The most surprising finding
was that the long-run abnormal return after three years was not significantly different from zero. This implied that the bidding firms did not under-perform relative to the market. This result stands in contrast to findings in other studies and it may reflect that earlier studies did not adjust correctly for the volatility component. These findings indicated that the market efficiency hypothesis is intact in the long run. It is only in the very short run, a few days around acquisition announcements, that the market makes a significant adjustment to uphold the efficiency hypothesis.

Andre, Kooli, and L'Her (2004) investigated the long-run performance of Canadian acquirers, using a sample of 267 acquisitions between 1980 and 2000. The study focused on two issues 1) the magnitude and reliability of abnormal returns and 2) the possible explanations of the long-term behaviour of M&A firms.

The main results were as follows First, focusing on a calendar-time portfolio approach and a WLS estimation procedure, the study found that the three-year post-acquisition returns for Canadian acquirers underperform significantly on an equal-weighted basis. Value-weighted abnormal returns were positive, but driven by a very large acquirer which participates in four transactions during the peak of the M&A wave. The mean monthly calendar-time abnormal returns (MCTARs) confirmed these observations. When they examined the case in which there is no overlapping, they found that Canadian acquirers significantly underperform over the three-year post-event period, whether they use an equal- or value-weight scheme.

Second, they examined possible explanations for the long-run performance of M&A deals. They found support for the extrapolation hypothesis, and for the method-of-payment hypothesis. Glamour acquirers underperformed relative to value acquirers and M&As financed entirely by equity underperformed relative to cash transactions. They also found that cross-border deals perform poorly in the long run. Although they found some explanations for the post-M&A performance in Canada, the issues raised and the complex nature of these transactions calls for further analysis.

Pangarkar and Lie (2004) hypothesize that acquisitions undertaken during low market cycles will exhibit better performance than other acquisitions for two key reasons lower likelihood of overpayment due to hubris and ease in implementing restructuring
initiatives such as retrenchment. They defined performance as the cumulative abnormal returns surrounding the acquisition event and deployed a trend-based measure for market cycle. Based on an analysis of 115 acquisitions by Singapore firms between 1990 and 1999, they found strong support for the hypothesized relationship.

Olson and Pagano (2005) studied the mergers of US publicly traded bank holding companies during 1987-2000. They identified the impact of bank mergers on the long run performance of the acquiring bank during 1987-2000 by analyzing 3-year cumulative buy-and-hold returns for each deal on a cross-sectional basis. They found that the acquiring firm's sustainable growth rate was an important determinant of the cross-sectional variation in the merged entity's long-term operating and stock performance. The most economically significant determinants of the merged bank's abnormal stock return performance were the acquiring bank's estimated sustainable growth rate prior to the acquisition, as well as post-acquisition changes in this growth rate, and the bank's dividend pay-out ratio. The findings are robust even after controlling for several potentially confounding factors.

Uysal (2005) scrutinized two important factors in M&A bidders' excess debt capacity and asymmetric information. First, he examined how leverage affects bidding behavior. He found that bidders which were underleveraged relative to their target debt ratios pay higher premiums than other bidders. Probability that they successfully acquire their targets was also found to be higher. Consistent with the free cash hypothesis, stock prices react more unfavorably to takeover announcements of underleveraged bidders.

Second, he empirically studied the role of asymmetric information in takeover contests. A large body of work suggests that better informed bidders have advantages in takeover contests. However, testing these theories is quiet difficult, as the informational advantage of bidders is typically unobservable. The approach used in this paper was to use geographical proximity between a bidder and a target. He found that (i) stock prices react more favorably to takeover announcements of local bidders; (ii) target shareholders of local bidders receive lower premiums; and (iii) locally merged firms show superior operating performance in the long run. These findings are
consistent with the idea that there is less asymmetric information between geographically proximate bidders and targets.

Yuce and Ng (2005) investigated the announcement effects of mergers and acquisitions on shareholders' returns between 1994 and 2000. The results showed that both the target and the acquiring company shareholders earn significant and positive abnormal returns for a two-day holding period starting with the announcement day. In the context of a worldwide merger boom during the 1990s and previous U.S. and Canadian studies, they found that mergers and acquisitions continue to benefit both target and acquirer firm shareholders. It was consistent with many findings that mergers do pay.

Their results showed that acquirers pay less for private companies than public companies, especially when they offer stock. They observed that risk-adjusted returns do not appear to differ substantially between these sub-samples of acquirers. Although Chang and Fuller et al. found higher returns to acquirers of private targets, they argued that these higher returns were negated by higher risk. Therefore, on a risk-adjusted return basis, there appeared to be no difference between buying private versus public targets. Overall, the findings suggested that the market can value acquisitions under asymmetric conditions with private firms.

Hassan, Patro, Tuckman and Wang Do (2007) examined short-term abnormal returns separating mergers from acquisitions and US-based from foreign-based M&A targets. It examined 405 mergers and acquisitions during 1981-2004 to address the issues of the research. Evidence of short and long-term abnormal returns, as well as accounting and efficiency effects were found for acquisitions but not for mergers. However, the tests do suggest that mergers with US-based targets were not value destroying. It was also found that there were differences as to the effects of acquisitions of foreign-based, as opposed to US-based targets. Taken in total, the results provide support for the view that in the pharmaceutical industry, acquisitions of US-based companies have a positive impact on wealth creation for company shareholders.

Oler (2008) investigated whether an acquirer's pre-announcement cash level can predict post-acquisition returns. This study revealed that acquisitions where the
acquirer had a high cash balance were likely to underperform (whether or not they are diversifying).

Overall, the results suggested that the market failed to fully incorporate the implications of the acquirer's cash level into its stock price around announcement. More investors seem to attend to the fundamental performance of the acquiring firm after the acquisition (proxied here by acquirer return on net operating assets).

Lensink and Maslennikova (2008) provided the first analysis of value performance of the European bank M&A wave of 1996–2004 that accompanied the general consolidation process of the European financial sector in the last decade. Using a sample of 75 publicly traded banks from 19 European countries, they examined gains to acquirers over five alternative periods ranging from 1 to 20 days upon the acquisition rumour. The results suggested that European acquirers earn positive and statistically significant abnormal returns around the time of the deal rumour/announcement. Partitioning the sample with respect to product-market and geographic diversification indicated strong statistical evidence that all types of domestic deals as well as bank-to-bank cross-border deals created shareholder value. Gains to cross-border diversifying deals were insignificant.

Sharma (2010) examined mergers and acquisitions in the United States banking industry involving the formation of mega banks. In this research he studied the cases of five mega mergers. Objective was to analyze whether these acquisitions pronounced success. Two techniques were used to examine the success of M&A. The first was the event study methodology, for which the target variables were abnormal stock price return (ASRP), cumulative abnormal stock price return (CASRP) and the Sharpe ratio. The second method was the accounting performance techniques, in which the target variables were return on equity (ROE), an indicator of profit, and the cash flow variables such as operating cash flow (OCF) and absolute cash flow (ACF).

Here the event study methodology tend to differ from accounting study methodology as event study has shown that value creation didn’t happen for any of the mergers whereas accounting study has shown that the value creation did happen for three out of the five mergers studied.
Sharma (2010) examined correlation between accounting and event study methodologies, which are used to analyze value creation in mergers and acquisitions. The study involved five mega mergers in the banking industry in the United States banking. The correlation process included using Pearson product moment correlation, non-parametric Wilcoxon test and multiple regression analysis. The study reflected only partial correlation can be found but no constructive relation could be established. This study did show that while there is partial correlation between these methods, a predictive relationship could not be established. These results imply, within the construct of this study, that accounting performance technique, as measured by ROE, OCF and ACF, are not significantly predictive of event study’s methodology, as measured by ASPRs.

Alexandridis, Petmezas, and Travlos (2010) used a global M&A data set and provided evidence that the empirical observations relating public acquisitions to, at best, zero abnormal returns, and their stock-financed subset to negative abnormal returns for acquiring firms around the deal announcement are not unanimous across countries. Acquirers beyond the most competitive takeover markets (the United States, United Kingdom, and Canada) pay lower premia and realize gains, while share-for-share offers are at least non-value-destroying for their shareholders. In contrast, target shareholders within these markets gain significantly less, implying that the benefits generated are more evenly split between the involved parties.

In this paper, they presented new evidence regarding the gains from public M&As to acquiring and target firms using a worldwide sample covering 39 countries from all continents. Accordingly, they first demonstrated that public acquisition announcements, in general, enhance acquirers’ value in countries beyond those with the most competitive takeover markets (the UUC). Acquirers within the latter markets significantly underperform those in the rest of the world. Second, they also provided evidence that deals financed with equity swaps do not overall destroy value for acquirers in countries beyond the UUC. One potential explanation for the nonnegative reaction in equity-financed public acquisitions within the Rest of the World (RoW) is that the negative information effect of an equity offer can, in practice, be subdued by the positive effect of lower premiums paid due to inferior competition. Third, they
found that RoW acquisitions were subject to superior synergy gains only for stock swaps, implying merely a redistribution of gains from the acquirer to the target in other types of transactions. Fourth, they examined the relationship between competition in the market for corporate control across time and markets and acquisition gains and premiums paid within the entire sample, as well as in the RoW and UUC subsets. Findings indicate that the level of competition is negatively associated with acquirer returns and positively associated with target returns and premia after controlling for other firm, deal, and market legal and institutional characteristics, as well as other country fixed effects. Overall, the paper provided evidence that public acquisitions do generate gains, but the distribution of gains between acquiring and target firms depends on the degree of competition in the market for corporate control. As a result, the empirical observations relating public acquisitions to, at best, zero abnormal returns, and their equity financed subset to negative abnormal returns for acquiring firms around the deal announcement are mainly limited to the most competitive acquisition markets.

Soongswang (2010) analyzed takeovers occurring on the Stock Exchange of Thailand (SET), focusing on the effects on successful bidding firms performances during a period of twelve months before the announcements. The study measured abnormal returns using an event study approach; applying two models and three parametric test statistics. The results suggest that the takeover effects are wealth-creating for successful bidding firm’s shareholders. Evidence was also found regarding the available takeover news being considered as good news in the market, four and three months prior to the announcement month, resulting in positive abnormal returns of approximately 17% and 10% for the bidders, as estimated from the market-adjusted and market models respectively.

Francis and Martin (2010) investigated if timely loss recognition is associated with acquisition-investment decisions. Using a piece-wise linear regression model, they found that firms with more timely incorporation of economic losses into earnings make more profitable acquisitions, measured by the bidder’s announcement returns and by changes in post-acquisition operating performance. These firms are also less likely to make post-acquisition divestitures (consistent with better ex ante investment
decisions). but act more quickly to divest. They also found that the positive association between timely loss recognition and acquisition profitability is more pronounced for firms with higher ex ante agency costs.

Liargovas and Repousis (2011) examined the impact of mergers and acquisitions on the performance of Greek banking sector over the period 1996-2008. The results from event study methodology, using a 30-day event window indicated that stock prices show significant positive cumulative average abnormal returns (CAARs) before the announcement for a period of ten days (for targets and bidders banks). Moreover, cash deals created more significant positive CAARs for bidder shareholders than stock deals, ten days before announcement. Also the results showed that significant positive CAARs were gained upon the announcement of horizontal and diversifying bank deals for target's shareholders. The overall results (the weighted average of gains to the bidder and target bank), indicated that bank mergers and acquisitions have no impact and do not create wealth. The empirical results also indicated significant implications for rejection of the "semi-strong form" of Efficient Market Hypothesis (EMH) of the Athens Stock Exchange, possibly reflecting leakage of information. By measuring twenty financial ratios, they found that the Greek banking industry is moderate and not highly concentrated (many banks with low market shares). Operating performance did not improve following mergers and acquisitions while there were controversial results when comparing merged banks with the group of non-merging banks.

Farinós, Herrero & Latorre (2011) investigated shareholder value creation of Spanish listed firms in response to announcements of acquisitions over the period 1991–2006. Similar to foreign markets, bidders earned insignificant average abnormal returns regardless of the pricing model used in the estimation procedure. When they related these results to company and transaction characteristics the evidence suggested that the listing status of the target firm was a critical key in the strategic decision to acquire a company. This listing status effect was mainly associated with the fact that unlisted firms tend to be smaller and lesser–known firms, and thus suffer from a lack of competition in the market for corporate control. Consequently, the payment of lower premiums and the possibility of diversifying shareholders’ portfolios lead to
unlisted firm acquisitions being viewed as value-orientated transactions which have major implications for managers.

Jayadev and Sensarma (2007) analyzed some of the critical issues of consolidation in Indian Banking with special emphasis on the views of two important stakeholders viz., shareholders and managers. First, they reviewed the trends in consolidation, in global and Indian banking. Then to ascertain the shareholder's view, they conducted an event study analysis of bank stock returns which revealed that in the case of forced mergers, neither the bidder nor the target banks' shareholders have benefited. However, in the case of voluntary mergers, the bidder banks' shareholders have gained more than those of the target banks. They conducted a survey of bank managers and in spite of absence of any gains to bidder bank, they strongly favoured mergers. The survey revealed that the critical issues in a successful merger are valuation of loan portfolio, integration of IT platforms, and issues of human resource management.

Ramakrishnan (2010) used a standard event study method and statistically analyzed share price and other secondary data. It was found that the acquired firm shareholders enjoy significant wealth gains of 11.6 per cent in a 21-day event window period, whereas the acquiring and combined firm shareholders do not do so. Mergers that do not see transfer of corporate control bestow significant wealth gains of 21.1 per cent on announcement on the target firm shareholders, whereas those where such a transfer takes place do not witness such gains.

Mann and Kohli (2011) used standard event study methodology has been applied to compute the announcement returns for domestic and cross-border acquisitions. Cross-border effect is calculated to compare the value creation in the two sets of acquisitions. Furthermore, cross-sectional regression analysis is conducted to capture the impact of bid-related features on target shareholder's value creation. The results indicated that both domestic and cross-border acquisitions have created value for the target company shareholders on the announcement. Nonetheless, the analysis of cross-border effect as well as regression analysis made it evident that value creation was higher for domestic acquisitions as compared to cross-border acquisitions due to the influence of various bid-specific factors. Thus, in India, bid-related variables are the
fundamental drivers of the target’s announcement wealth gains irrespective of the nationality of the acquirer.

When we reviewed the studies done in the other countries specifically US and Europe, the results showed improvement in many studies. However some of these studies show either poor or average performance. The collective number of studies showing average and poor performance was equal to the number of studies showing post-merger improvement in performance. Further when the researches done in Indian context are reviewed, the results found are similar to those of US and European studies.

Because the analysis does not lead to strong conclusion regarding the impact of M&A on firm performance, it is important to analyze a large sample of merged companies from all the possible perspectives. Because it lead to the question that why some studies report M&A as a successful tool for firm growth while some other report poor post-acquisition performance? It implies that there are some underlying factors which make some deals successful and others futile. Therefore performance of combined entities should be measured by grouping them on the basis of payment method, size, relatedness or strategic fit, group vs. non group mergers, single vs. multiple acquisitions etc. This type of analysis may be helpful to identify the factors which make M&A an effective growth strategy.

Another aspect of the literature review is that these studies have used cumulative abnormal returns, accounting ratios and cash flows as performance measures. When the results of several studies were analyzed with reference to the methods of performance evaluation used, following facts were found

- Event studies have shown mixed results for other countries and favorable results in Indian context.
- Accounting studies have shown mixed results for Indian as well as other economies.
- Cash flow based studies have shown favorable results for Indian as well as other economies.
From these results of previous studies we can infer that choice of method of performance evaluation may influence the results of the study. Therefore it is important to apply the different methods on the same sample to know the difference in performance measurement caused by the choice of method.

Whereas examining long-term stock returns has been a popularly used approach, the use of accounting and financial data is appropriate to measure directly post-acquisition operating performance gains. Traditional accounting rate of returns and profitability measures are criticized for their deficiencies in measuring performance, particularly because they ignore capital costs and have the potential for manipulation of accounting data. A new performance measure, EVA, overcomes these flaws existing in conventional financial metrics as a true performance measure. Therefore it will be fruitful to analyse the same sample by applying EVA as a measure of performance, in addition to accounting ratios and cashflows.

2.3 Impact of mode of payment on the performance of M&A

Meliaher and Harter(1972) found that, on the average, acquisitions characterized by the acquired company as being more than one-half the size of the acquiring company exhibited significantly higher price increases than companies engaging in smaller relative-size acquisitions.

The method of financing and acquisition activity characteristics Indicated possible significance over the three months post-merger to six months post-merger period. Common stock financed acquisitions were characterized, on the average, by a decrease in trend-adjusted stock prices over the second post-merger quarter in contrast to an increase for non-common stock financed acquisitions. Likewise, non-active acquirers suffered a price decrease over the second post-merger quarter in contrast to an increase for the active acquirers. Companies financing acquisitions with non-common stock securities probably were able to diminish or avoid post-merger dilution in earnings per shares and acquisition-oriented companies seem to have been able to avoid the post-merger stock price let-down by entering into additional acquisitions.

Wansley, Lane and Yang (1983) tested abnormal returns to shareholders of acquired firms around the day of merger announcement for systematic differences across
merger types (non-conglomerate, other conglomerate, and pure conglomerate) and payment method (cash, securities, and combinations). Significant differences in abnormal returns appeared to exist, however, when the mergers were compared by payment method. Seller shareholders in cash acquisitions earned, on average, 33.54 percent abnormal returns from 40 days prior to the original merger announcement through the announcement day. This figure was almost twice the corresponding number (17.47 percent) for mergers employing securities as the medium of exchange. They attributed this difference to a tax effect, regulatory requirements that favor cash as the medium of exchange, and the increasing popularity of cash mergers during a period of generally higher premiums associated with all mergers.

Cornett and De (1991) examined the role of medium of payment in corporate acquisitions with the help of evidence from a large sample of interstate bank mergers which took place over the five-year period from 1982 through 1986. The results of this study indicated that when the full sample of banks involved in interstate bank mergers was divided into subsamples by medium of payment the abnormal announcement period returns for the subsamples were found to be equal to each other, as well as to the results for the full sample. The finding that bidder returns are not affected by the bidder's choice of medium of payment is in contrast with findings of the existing empirical studies that have explored this issue in the context of nonbank mergers (Asquith, Bruner, and Mullins 1987; Travlos 1987; Eckbo and Langohr 1989; Franks, Harris, and Mayer 1988). They all report significantly higher bidder returns from cash-financed acquisitions than from stock-financed acquisitions.

Nayar and Switzer (1998) examined the use of debt in the payment package employed by bidding firms for corporate acquisitions. They compared the announcement period stock price reactions for 41 bidding firms that incorporated some debt in the total consideration paid to target shareholders with reactions for a large sample of bidders that used internally generated cash, all stock, or some combination of cash and stock offers. The evidence indicated that the bidder's stock price reaction was associated with the riskiness of the debt, the ability to benefit from the tax shield afforded by the interest payments, and the amount of stock included in the offer together with the debt. The results were consistent with the notion of optimal risk sharing/capital
structure realignment by the bidding firm. Their results provided an insight into the issue of how firms should pay for acquisitions. They stated that if firms want to avoid the diverse selection costs associated with a pure equity offer but desire to obtain contingent pricing and tax benefits, they should use debt as a part of the payment medium to target shareholders. They should balance the increased use of debt by also employing some equity if the pre-existing debt levels are high.

Heron and Lie (2002) analyzed the relationship between operating performance and the method of payment in takeovers. They used a large sample of acquisitions announced and completed between 1985 and 1997. When they categorized the sample according to payment type, they found no difference in the pre-acquisition discretionary accruals or post-acquisition changes in operating performance across payment categories. These results persist in a multivariate framework. Consequently, the method of payment does not appear to provide information regarding the firms' future operating performance. Instead, they found that improvements in operating performance subsequent to acquisitions were significantly greater when firms with higher market-to-book ratios acquired firms with low market-to-book ratios and when the acquirer and target belong to the same industry.

Sudarsanam and Mahate (2003) examined the effect of different acquirer types on their short and long term performance. (1) the performance of acquirers, both in the short- and long-run, using a variety of benchmark models; (2) whether the short- and long-run performance of acquirers is dependent on their pre-bid status as glamour or value acquirers, measured by the PE ratio and MTBV; (3) the interaction between the acquirer status and the method of payment used by acquirers (in particular, they argued that glamour acquirers are more likely to use equity as a method of payment and value acquirers to use cash); and (4) whether the pre-bid financial status or the method of payment dominates long-run performance of acquirers. Their sample included 519 UK takeovers completed between 1983 and 1985.

They provided some support for the argument that glamour firms are more likely to use equity financing than cash. Value acquirers are more likely to use cash. Glamour acquirers offering equity seriously underperform than those offering cash. They found that Irrespective of their pre-bid financial status, cash paying acquirers generate
higher returns for their shareholders than equity offering acquirers in the three year, post-acquisition, period.

Limmack (2003) worked on the paper by Sudarsanam and Mahate (2003) While Sudarsanam and Mahate find that glamour stocks consistently underperform value stocks in the long-run following takeovers, they nevertheless find that, on average, value stocks also record significantly negative abnormal returns. The authors also report that glamour acquirers are more likely to use a pure equity offer than a pure cash offer, consistent with the use of 'over-valued' equity. The final result reported by the authors was that the cash-financed bids outperform equity-financed bids, both for glamour and value acquirers.

Dhiensiri, Sahin and Sarajoti (2011) investigated how the equity-based compensation (EBC) of top executives affected the performance of acquisitions. In contrast to the results of Datta et al. (2001), they found that high EBC acquirers pay higher premiums for targets than that of low EBC acquirers. The cumulative abnormal return around the acquisition announcement was lower for acquiring firms with high EBC. However, they found that the long-run performance of acquiring firms was positively correlated with EBC. The results suggested that high EBC acquirers experienced lower sensitivity to size and momentum factors that unexpectedly lowered the cost of equity, leading to higher returns.

Mann and Kohli (2009) examined the effect of mode of financing employed in mergers and acquisitions on the announcement period returns of the acquiring and the target companies' shareholders in India. They found that maximum value has been created for the shareholders of the target companies engaged in cash offers followed by the shareholders of acquiring companies engaged in cash offers, target companies engaged in stock offers, and lastly, for acquiring companies engaged in stock offers.

Ramakrishnan (2010) analyzed the performance of merged companies and factor influencing it. Pre-tax operating cash flow deflated by the operating assets was used to measure firm Performance The raw firm operating performance figures calculated were adjusted for industry and economic effects. The change in performance on
account of the merger was captured by comparing the post and pre-merger performance measure.

He concluded that mergers have enhanced the long-term performance of firms in India. This improvement was on account of higher efficiency of utilization of assets. Unrelated mergers appeared to be performing better in the long term, contrary to strategic management theory. The relative size of the acquired firm and the method of payment did not seem to be playing a significant role in influencing post-merger returns.

The studies which have investigated the phenomenon of impact of method of payment on the post-acquisition performance of firms are small in number and have given mixed results. Few have concluded that non-common stock financed mergers perform better while some other studies have concluded that there is no impact of method of payment on performance. Some studies have favoured the stock as a medium of payment. Very few studies were available in Indian context which have studied the impact of medium of payment on M&A performance. One of these research work concluded that mergers which have used cash as a medium of payment have performed better. Another study concluded that method of payment did not seem to be playing a significant role in influencing post-merger returns. Because not much work has been done in India in this direction therefore it is important to evaluate this aspect of M&A in Indian context.

2.4 Impact of size of the target firm on the performance of M&A

Melicher and Harter (1972) found that, on the average, acquisitions characterized by the acquired company as being more than one-half the size of the acquiring company exhibited significantly higher price increases than companies engaging in smaller relative-size acquisitions. The near total significance of the relative asset size variable seemed to bear out a priori expectations. When a company acquires another company approaching its size (or even larger), significant immediate growth in book values, earnings, and often earnings-per-share figures can be created through the "pooling-of-interests" accounting method. In addition to the immediate altering of the acquiring company's financial statements, the potential impact of longer-run operating synergies would be expected to be greater in contrast to the acquiring of relatively smaller
companies. Finally, the publicity surrounding the merger of relatively large companies might lead to generally greater speculation and anticipation.

Dutta (2006) empirically examined the short and long-term performance, and the differentiating characteristics of acquiring firms by using a comprehensive sample of 1300 Canadian acquisition events during the period of 1993-2002. With respect to short-term abnormal returns, they found significant and positive abnormal returns for Canadian acquiring firms' shares around the announcement date. With respect to long-term stock return performance, they found no strong support for positive long-term abnormal returns for acquiring firms that was robust across all methodologies. They also do not found any improvement in long-term operating performance in general. However, they found that long-term operating performance increases significantly for the relatively larger deals and the market reacts more favourably to those deals around the announcement date. This implies that only relatively larger deals bring economically significant benefits to the acquiring firms and market recognizes this aspect.

Ramakrishnan (2010) analyzed the performance of merged companies and factor influencing it. He concluded that mergers have enhanced the long-term performance of firms in India. This improvement was on account of higher efficiency of utilization of assets. Unrelated mergers appeared to be performing better in the long term, contrary to strategic management theory. The relative size of the acquired firm and the method of payment did not seem to be playing a significant role in influencing post-merger returns.

The studies which have evaluated the impact of size are very limited. In India very small number of studies are found which has probed this aspect of M&A performance. One of the study concluded that the relative size of the acquired firm did not seem to be playing a significant role in influencing post-merger returns.

The studies from other economies have resolved that if the size of the target is big then the benefits of mergers are more probable to occur and more visible. However few studies have resolved that if the size of acquired firm is small then post-merger integration is effective and will lead to better performance. One of the research works
has also thrown the light on the impact of size of acquirer. It concluded that small size acquirer is likely to make successful acquisitions because of the less probability of overpayment by them. Because this facet of M&A performance is almost untouched in Indian context therefore it is important to evaluate the sample from this perspective too.

2.5 Comparison in the performance of related and unrelated M&A

Wansley, Lane and Yang (1983) tested abnormal returns to shareholders of acquired firms around the day of merger announcement for systematic differences across merger types (non-conglomerate, other conglomerate, and pure conglomerate) and payment method (cash, securities, and combinations). Contrary to their original expectations that returns to seller shareholders are larger in horizontal or vertical mergers than in conglomerate mergers, they found that pure conglomerate acquisitions are associated with slightly larger, although not significantly larger, CAR to the shareholders of the acquired firms.

Seth (1990) re-examined the following research questions towards resolving the inconsistent findings

1. Do acquisitions result in the creation of economic value?
2. Are different acquisition strategies associated with different degrees of value creation?

This study used the event study methodology as the basis for estimating synergistic gains in acquisitions. The time-series of combined returns were used to estimate pre acquisition market model coefficients, for each pair of combined firms. The sample consisted of 104 tender offers for control which took place between 1962 and 1979. Regardless of the basis of classification, both unrelated and related acquisition strategies have been shown to create significant synergies, in accordance with the expectations. He mentioned that the data do not appear to indicate that related acquisitions create more value than unrelated acquisitions on average.

Datta and Grant (1990) examined the degree of autonomy provided by acquiring companies to the management of acquired firms in the managing of post-acquisition
operations as well as the relationships between such autonomy and the perceived success of the acquisition. Results showed that in unrelated acquisitions the extent of autonomy was significantly greater than in related acquisition. Also it was found that autonomy was positively associated with superior performance in unrelated acquisitions, but the relationship was not significant in related acquisitions. They stated that future studies should incorporate factors related to post-acquisition managerial decisions and organizational fit.

Chatterjee (1991) investigated the factors that can explain the gains resulting from vertical mergers. The findings suggest that acquiring firms gain the most when they come from concentrated markets and target firms come from fragmented markets. The findings also suggest that, on the average, the firms studied increased their market power as a result of mergers.

Healy, Palepu and Ruback (1997) examined acquiring companies' cash flow performance after a merger in the fifty largest U.S. industrial takeovers from 1979 to mid-1984. In an earlier study, they showed that the mergers in this same sample created new value for the stockholders of the target company and the acquiring company combined. But their results here showed that the acquirers did not generate any additional cash flows beyond those required to recover the premium paid.

However, while the takeovers were break-even investments on average, the profitability of the individual transactions varied widely. There were two distinct types of takeovers in their sample (1) friendly transactions that typically involved stock payment for firms in overlapping businesses, which they called "strategic" takeovers; and (2) hostile transactions that generally involved cash payments for firms in unrelated businesses, which they labeled "financial" takeovers.

They also examined the relation between the profitability of takeover transactions and three transaction characteristics that management controlled. Those characteristics were (1) the target managers' attitude, (2) the form of payment, and (3) the degree of overlap of the merging firms' businesses. Paired comparisons showed that friendly takeovers outperformed hostile takeovers, acquisitions with stock payment outperformed cash transactions, and takeovers with a high overlap between acquirers
and target companies performed better than those of unrelated businesses. Each comparison showed superior performance because of both higher takeover synergies and lower premiums paid to the stockholders of target companies. These results suggested that the transaction characteristics that were under management control substantially influenced the ultimate payoffs from takeovers.

Ramaswamy and Kannan (1997) examined the impact of strategic similarities between target and bidder firms on changes in post-merger performance. Set in the U.S. banking industry, the empirical examination showed that mergers between banks exhibiting similar strategic characteristics resulted in better performance than those involving strategically dissimilar banks.

Capron (1999) examined how value is created in horizontal mergers and acquisitions. More specifically, he examined the impact of post-acquisition asset divestiture and resource redeployment on the long-term performance of horizontal acquisitions. The data came from a detailed survey of acquiring firm managers and covered 253 horizontal mergers and acquisitions that were initiated by European and U.S. firms in manufacturing industries for the period 1988-1992. Overall, results showed that both asset divestiture and resource redeployment can contribute to acquisition performance, with, however, a significant risk of damaging acquisition performance when the divested assets and redeployed resources are those of the target.

DeLong (2001) stated that bank mergers that enhanced value upon announcement can be distinguished from those that did not create value. He classified mergers of banking firms according to activity and geographic similarity (focus) or dissimilarity (diversification), and examined the abnormal returns to each group as a result of the merger announcement. Mergers that focused both activity and geography enhanced stockholder value by 3.0% while the other types did not create value. Analysis revealed that abnormal returns upon merger announcement increased in relative size of target to bidder, but decreased in the pre-merger performance of targets.

Park (2002) examined the possible influence of a firm's prior performance on its choice between related and unrelated acquisition. This paper presented the evidence that firms in high-profit industries tend to pursue related diversification whereas firms
in low-profit industries follow unrelated diversification. Therefore, related diversifiers are more profitable than unrelated diversifiers, partly because they were in higher-profit industries prior to diversification than unrelated diversifiers. That is, there is a spurious correlation between diversification strategy and profitability, which is caused by prior industry profitability.

This paper thus suggested that related diversifiers are more profitable than unrelated diversifiers are, because related diversifiers were not only active in higher profit industries but also were more profitable within their industries than unrelated diversifiers, prior to diversification. Therefore, related diversifiers are characterized as firms in profitable industries and/or profitable firms within their industries prior to diversification, whereas unrelated diversifiers are characterized as firms in less profitable industries and/or less profitable firms within their industries prior to diversification.

The results showed that related acquisition was not positively related to post-acquisition firm profitability. This confirms that higher profitability of related acquisition was primarily due to the two types of spurious correlation, not to the superiority of related acquisition over unrelated acquisition.

Yeh and Hoshino (2002) investigated the effects of mergers on the firms’ operating performance and the Keiretsu’s roles in the performance variation. This was motivated by the contradicting arguments whether Japanese Keiretsu can effectively control agency conflicts and increase firm efficiency. Examining 86 Japanese corporate mergers completed from 1970 to 1994, they found that (1) Japanese mergers failed to improve the firm efficiency, and even caused deterioration in the firms’ operating performances; (2) the Keiretsu relationship was particular detrimental to the merging firms’ post-merger performance.

Park (2003) focused on a single event of a large acquisition, which enabled him to better identify the sequential relationships between prior firm profitability, prior industry profitability, and subsequent acquisition strategies. This paper has presented two findings (1) related acquirers were more profitable in their industries than
unrelated acquirers, prior to acquisition; and (2) related acquirers were in more profitable industries than unrelated acquirers, prior to acquisition.

Kim and Finkenstein (2009) investigated the effects of strategic and market complementarity on acquisition performance in the context of related horizontal acquisitions. They also proposed that two key attributes of acquirers—strategic focus and out-of-market acquisition experience—will moderate this relationship. They investigated the research questions in the context of all 2,204 acquisitions made by publicly traded U.S. commercial banks during the 12-year period from 1989 to 2001. Their findings are generally supportive, suggesting complementarity is an important antecedent of acquisition performance, and raising important issues on the nature of acquisition research in general.

Laabs and Schiereck (2010) examined the short- and long-term wealth effects of horizontal mergers and acquisitions on acquirers in the automotive supply industry. Based on a sample of 230 takeover announcements between 1981 and 2007, significant positive announcement returns to acquiring companies were determined. This study also found that acquirers were unable to sustain this exceptional position beyond a short-term horizon. A combination of the Fama-French-3-Factor model in calendar time and the control firm approach in event time consistently revealed significant value destruction of about 20% over 3 years. The influence of product diversification remained inconclusive and could not ultimately be determined in this study.

Shim, Jeungbo (2011) examined the relationship between mergers & acquisitions, diversification and financial performance in the U.S. property-liability insurance industry over the period 1989-2004. The risk-adjusted return on assets (ROA), return on equity (ROE), Z-score and total risk measured by earnings volatility were considered as a relevant indicator of performance. They found that acquirers' financial performance decreased and earnings volatility increased during the gestation period after the M & As perhaps due to increased frictional costs associated with post-merger integration and agency problems. They found that more focused insurers outperformed the product-diversified insurers, implying that the costs of
diversification outweigh the benefits. These findings were robust to alternative risk and diversification measures.

Ramakrishnan (2010) analyzed the performance of merged companies and factor influencing it. The change in performance on account of the merger was captured by comparing the post and pre-merger performance measure.

He concluded that mergers have enhanced the long-term performance of firms in India. This improvement was on account of higher efficiency of utilization of assets. Unrelated mergers appeared to be performing better in the long term, contrary to strategic management theory.

Enormous work has been done in foreign countries for comparing the performance of related and unrelated acquisitions. Majority of the research work has favoured the relatedness or strategic fit or complementarity as an important factor towards the M&A success. Again in Indian context this issue has been scrutinized only by very few studies. This study concluded that unrelated mergers appeared to be performing better in the long term, contrary to strategic management theory. In the light of negligible work done in India, it will be fruitful for the industry to know that which type of acquisitions leads to better performance. Therefore there is a need to subdivide the sample into related and unrelated M&A and compare their performance.

There is another view also expressed by some researchers that it is not relatedness which leads to better performance rather it is other way round. Firms in high-profit industries tend to pursue related diversification whereas firms in low-profit industries follow unrelated diversification. Therefore, related diversifiers are more profitable than unrelated diversifiers, partly because they were in higher-profit industries prior to diversification than unrelated diversifiers. Specifically, this paper showed that high-profit firms within their industries tend to pursue related diversification, whereas lower profit firms seek unrelated diversification. Therefore, related diversifiers are more profitable than unrelated diversifiers, partly because they were more profitable within their industries prior to diversification than unrelated diversifiers. Therefore it may be useful to see the impact of industry profitability on the type of acquisitions.
taking place in that industry. Keeping in view the quantum of work required for this purpose, this aspect may be probed in future researches.

2.6 Impact of capital structure of acquirer on M&A performance

Pantalone and Platt (1993) focused on the risk and return performance of savings and loans that were active acquirers during the early and mid-eighties relative to that of non-acquirers. Acquirers took on more risks than non-acquirers, but were less profitable. Separating acquirers by the health of their acquisitions, acquirers of both healthy and troubled associations or of troubled associations only were more highly leveraged and saw their profitability erode over the post-acquisition period. While in case of acquirers of only healthy associations capital ratio was similar to that of non-acquirers, they maintained a more aggressive financing position. That is, acquirers relied more heavily on borrowed money to finance their assets than did non-acquirers. However, they also had the highest net operating margin of the four groups. While acquirers of only healthy associations were more aggressive than were non-acquirers, they compensated for this higher risk by higher operating profit margins.

Uysal (2005) examined how leverage affects bidding behaviour. This is an issue that has generated considerable interest—his departure from the existing literature was that he considered how takeover activity was influenced by the acquiring firms' deviation from their target capital structures. He found that bidders which were underleveraged relative to their target debt ratios paid higher premiums than other bidders. Probability that they successfully acquire their targets was also found to be higher. Consistent with the free cash hypothesis, stock prices reacted more unfavourably to takeover announcements of underleveraged bidders. In addition, leverage deficit subsumes effects of leverage and excess cash reserves which have been shown to be important determinants of bidding behaviour and stock price reactions.

Oler (2008) investigated whether an acquirer's pre-announcement cash level can predict post-acquisition returns. This study revealed that acquisitions where the acquirer had a high cash balance was likely to underperform (whether or not they are diversifying). There are some limitations to this research. Sample included only acquisitions where the acquirer and target were public firms with share price data.
available on CRSP and financial statement data available on Compustat. Only acquisitions where the target was 100 percent acquired were considered. Further research could investigate whether findings can be generalized to acquisitions where a minority interest remains publicly traded and acquisitions between public and private firms.

The existing research work has not paid much attention to impact of capital structure of acquirer on acquisition performance. Such studies have inferred that underleveraged bidders pay higher premiums. Their negative stock performance is consistent with free cash flow hypothesis. High cash levels of acquirers have also lead to underperformance of such bidders. While the aggressive acquirers with higher debt levels are found to be compensating for this risk by higher operating performance. One of the contrary views is that value is created when firms with low financial leverage acquire firms with high financial leverage. Firms with unused debt capacity may be able to create value by using financial slack to acquire other firms. A low debt-to-equity or a low interest-expense to earnings ratio indicates the ability to service more debt. Value is created because slack rich bidders can pursue the profitable but unfunded investment opportunities of the previously slack poor targets. It is therefore important to see whether there is a difference in the performance of M&A deals where acquirer has low vis-à-vis high debt in its capital structure, prior to acquisition. It could be an interesting area to search the impact of capital structure of bidders on acquisition performance.

2.7 Impact of promoter's stake and group/non-group mergers & acquisition on the post merger performance

Lane, Alberta and Michael (1998) mentioned that Amihud and Lev (1981) are widely cited as providing evidence that managers, unless closely monitored by large block shareholders, will attempt to reduce their employment risk through unrelated mergers and diversification. These corporate strategies, however, may not be in shareholders' interests. Reconsidering the agency assumptions underlying Amihud and Lev's study and the methodology they used, the researchers developed hypotheses regarding the association between ownership structure, board vigilance, corporate strategy, and corporate performance from management theory and tested them using
Amihud and Levy’s data from the 1960s and new data from the 1980s. Neither study supported the conclusions of Amihud and Levy, nor the agency theory belief that monitoring efforts by principals affect the strategic behaviors of agents or the performance of firms that they manage.

Yen and Andre (2007) provided empirical evidence on the relation between concentrated ownership and the long term operating performance of acquiring firms. They investigated the performance around 287 takeovers in English-origin countries other than the US by following the classification of La Porta et al. Their principal finding was that the relationship between concentrated ownership and the level and change in operating cash flow returns after takeovers is non-linear. Value creating deals were associated with higher levels of concentration consistent with decreasing agency costs as the dominant shareholder’s wealth invested in the acquiring firm increases.

Feys and Manigart (2011) analyzed the post-acquisition performance of 384 unquoted owner-managed firms that have been acquired between 2000 and 2004, and compare it with 875 comparable, but independent owner-managed firms. It was shown in the paper that target firms in domestic acquisitions were less profitable and grow less than independent firms, both before and after the acquisition. Target firms in cross-border acquisitions were comparable to independent firms in growth and profitability, but they have higher margins and higher returns after the acquisition. Hence, findings indicated that especially cross-border acquisitions created operational synergies.

Pawaskar (2001) studied 36 mergers that had taken place in India between 1992 and 1995, using accrual measures of accounting spread over three years before and after the merger. The study found that the profitability of the merged firms was impacted negatively due to the merger, i.e., corporate performance did not improve significantly post-merger. A majority of the mergers studied in this paper were between companies belonging to the same business group, carried out as part of corporate restructuring. This might make the result quite specific and not generalizable. In addition, the study used matched companies as controls for both the acquiring and acquired companies. But, when a majority of the mergers studied are within-business group mergers, it is imperative that even the control pairs be from
similar groups. This would ensure similarity in terms of their situation within the industrial and economic context, as also a modicum of overlap in the merger motivations. Since, this had not been considered in the paper, along with the fact that getting such control companies may be well-nigh impossible, the study had serious limitations in terms of validity and generalizability of the results.

Mann and Kohli (2009) explored the following aspects of group mergers and acquisitions To discern the probable reasons for the positive value being created in within-group stock offers especially for the acquiring companies' shareholders, the second section analyzed the interaction between the announcement returns of the acquiring and the target companies engaged in stock offers and insiders'/promoters' ownership level.

The analysis revealed that the within-group stock offers have created value with increase in level of ownership with maximum value being created when controlling shareholders' ownership reaches the highest level (the category OWN> 49%). Likewise, not only acquiring companies' but the target companies' shareholders have gained positive returns. It means the stock market has reacted positively to the news of stock offers when these are undertaken by companies belonging to the same group as well as when the ownership is concentrated in the hands of promoters. Therefore they deduced that in India, within-group stock offers were not aimed at tunneling of resources by the acquiring companies; rather these were aimed at creating value by providing an internal market where the group companies can pool their resources and hence can create various kinds of synergies in the post-acquisition period. Hence, the results were in consonance with the value added view.

Mongla and Singh (2011) analyzed a sample of 170 companies merged in India during the period 1993-2003. Total sample has been classified into two sub-samples, that is, group mergers (125) and non-group mergers (45). Operating performance of three pre-merger years was compared with three post-merger years and thereby the outcomes of the mergers were discussed. The result showed that profitability has declined in the post-merger period in both group and non-group companies. However non-group mergers have shown much greater decline in return on net worth and negative net profit margin in the post-merger period. Group mergers have attained
operating efficiencies in terms of reduced cost of production to net sales in post-merger period, whereas non-group mergers have lost their edge over operational synergies. Significant decline has been observed in EPS during the post-merger period in the sub-sample of non-group mergers. The reason for this decline was operational inefficiency and poor asset utilization by non-group merged companies. The study provided evidence that group mergers are a better choice than non-group mergers.

Previous research work has also touched the impact of ownership concentration and group vs. non-group mergers on merger performance. Though few studies have been done in this area but they have supported the view that the owner controlled firm exhibit superior post-acquisition performance. Similarly group mergers were also found to be beneficial. However limited literature available on this subject compels us to probe this issue on our sample.

2.8 Performance of multiple mergers & acquisitions

Fowler & Schmidt (1989) extended previous research efforts and examined relationships between commonly discussed strategic acquisition factors and long-term financial performance measures of acquiring firms. The financial performance measures included both accounting and capital market data for the 4-year period preceding acquisition activity and the 4-year period following such activity. The study presented bivariate and multivariate analyses for 42 industrial manufacturing firms that engaged in the tender offer form of acquisition. The findings indicated that, on the average, post-acquisition financial performance improved significantly for organizations that had previous acquisition experience, acquired a higher percentage of target, or were older. Post-acquisition performance decreased significantly for acquiring firms when target firms contested an acquisition.

Halebian and Finkelstein (1999) examined the influence of prior organizational acquisition experience on the performance of acquisitions. The behavioural learning theory, which examines both the conditions preceding organization events and organizational responses, predicts that experience effects may range from positive to negative. To test the hypothesis they applied event study analysis on a sample of 449 acquisitions. To explore the study's hypotheses further, and to enhance the robustness of the results, they conducted three different supplementary analyses (1) one using an
accounting-based acquisition performance measure, (2) a second that examined the effects of recent acquisition experience, and (3) an investigation of experience effects at the individual level of analysis. Consistent with this theory, data from 449 acquisitions showed an overall U-shaped relationship between organization acquisition experience and acquisition performance. In addition, the more similar a firm's acquisition targets are to its prior targets, the better they performed. These findings suggested that relatively inexperienced acquirers, after making their first acquisition, inappropriately generalize acquisition experience to subsequent dissimilar acquisitions, while more experienced acquirers appropriately discriminate between their acquisitions. Behavioral learning theory, then, may enhance understanding of organization experience effects.

Hayward (2002) used an organizational learning perspective to examine how the nature, performance and timing of a firm's acquisition experience helps it to learn how to select the right acquisition. He predicted the performance of 214 acquisitions made by 120 firms in 6 industries between 1990 and 1995. Results revealed that a firm's focal acquisition performance positively relates to prior acquisitions that are a) not highly similar or dissimilar to the focal acquisition, b) associated with small losses and c) not too temporally close to or distant from the focal acquisition. Taken together, these results identify the broad conditions in which firms generate adaptive and timely inferences from acquisition experience. Findings here suggested that such experience is a necessary but not sufficient condition for acquirer learning. Learning also requires attention to the nature, performance and timing of experience (March, 1991; Penrose, 1959). This contrasts with advice that firms should 'stick to their knitting' by undertaking a series of highly related acquisitions (Porter, 1987, 1996; Ravenscraft and Scherer, 1987). This latter strategy may work for a while, but tends to fail when market conditions change. Instead, here results are closer to evolutionary thinking that firms benefit from a variety of experience, experimenting and temporal rhythms (e.g., Brown and Eisenhardt, 1997). In this view, acquirers develop specialist skills to exploit their existing opportunities and generalist skills to explore new ones.

Finkelstein and Haleblian (2002) examined positive and negative transfer effects in organization acquisitions. Data from 96 organizations revealed that, consistent with
theories on positive transfer of industry knowledge, similar acquisitions are positively related to acquisition performance. In addition, consistent with theory on negative transfer of past acquisition knowledge, second acquisitions underperform first acquisitions, particularly when first and second targets are from different industries.

Haleblian, Kim & Rajagopalan (2006) drew upon theories of organizational learning to examine acquisition likelihood in a sample of banking industry acquisitions from 1988 through 2001. Their findings are consistent with their theoretical predictions (1) prior acquisition experience, (2) recent acquisition performance, and (3) the interaction between acquisition experience and recent acquisition performance are all positively related to the likelihood of subsequent acquisition. In conclusion, their study provides useful insights into the effects of learning from experience and performance in the context of corporate acquisitions.

Laamanen and Keil (2008) analyzed the most active acquirers in seven industry sectors in the United States in the 1990s. They found that both a high rate of acquisitions and a high variability of the rate are negatively related to performance. An acquirer’s size, the scope of its acquisition program, and acquisition experience moderate the relationship by weakening the negative effects.

It is the timing of acquisitions that determines whether experience or indigestion effects end up dominating (Hayward, 2002). Research findings suggest that over time, active acquirers develop such program level capabilities for managing their acquisition programs as they learn what is the optimal number of firms to acquire, how to time individual acquisitions, and what types of firms to acquire.

Ng (2009) stated that, although the effects of multiple acquisitions are studied with daily abnormal returns, none examine long term effects. Growth maximization (Mueller, 1972) is uniquely suitable as a managerial motivation for frequent acquisition activity. This motivation was examined through the operating and market performance of 138 frequent acquirers during 1996-2000 in Canada. Results showed that frequent acquirers experienced significant deterioration in operating performance.

Buckley, Elia and Kafouros, (2011) dealt with acquisitions from emerging to advanced countries and the performances of the target firms. The results showed that
EMNCs did not always acquire firms with a high pre acquisition performance and that they did not significantly increase the post-acquisition profitability of the target firms. They also showed the importance of the acquisition experience of the acquiring firms. Experienced EMNCs not only acquire firms with a higher pre acquisition performance, but also contributed to increase more significantly the productivity and sales of the target firms.

Kumar and Rajib (2007) analyzed a sample of 53 firms involved in multiple mergers during the period 1993-2002. This study aimed to analyse the financial characteristics of firms that engaged in multiple mergers. (In this context multiple mergers are mergers in which acquiring firms have engaged in three or more mergers.) The study attempted to determine the characteristics of the acquiring firms and observe whether multiple merger firms showed superior corporate performance compared to a matched control group.

A total of 53 firms involved in multiple mergers (the minimum number of mergers was taken as three) based on industry sectors were selected for the study and the data was collected for roughly a ten-year period, 1993-2002. Non-parametric tests like the Mann Whitney test and the Kolmogorov Smirnov test were used to study the comparative differences between the average of the two groups. Finally a logit model was applied to measure the probability of acquisition as a function of the financial characteristics of the multiple merger acquirer firms.

Their results indicated that low financial leverage and unused debt capacity would be a motive for firms to use multiple mergers as a strategic business tool. Thus a firm's capital structure appears as an especially important variable in the decision to go in for multiple mergers. Larger firms having large resources in terms of financial strength are likely to undertake multiple mergers. The results suggested that mergers were used to maximise the size of firms and to revitalise the bidding companies. Firms with low debt levels and free cash flows may incur agency costs by investing in multiple merger activity. Multiple mergers could also become a tool to increase the management’s efficiency in producing sales per value of assets. Firms where the power of the main shareholder is low are more likely to involve in multiple mergers. A
limitation of the study was that it included only those companies that survived after mergers. Hence there is the possibility of survivorship bias in the sample.

Whatever research work has been done in the area of impact of multiple mergers on the success of subsequent merger favours the argument that multiple mergers lead to learning by the management of acquirer firm. Though largely the research work favours the learning by active acquirers, there are many underlying issues which may affect the conversion of learning into acquisition success. For example the multiple mergers were of same type or there was diversity among the previous deals. Was there consistency or there were alternate episodes of active acquisitions and silence. However scanty research work is found in this area in Indian context and that does not support the argument that multiple mergers positively impacts the acquisition performance. One of such concluded that firms with low debt levels and free cash flows may incur agency costs by investing in multiple merger activity. Multiple mergers could also become a tool to increase the management’s efficiency in producing sales per value of assets. Firms where the power of the main shareholder is low are more likely to involve in multiple mergers. Thus again this phenomenon has to be tested for the emerging economy like India.

The review of literature has provided great insights into the phenomenon of evaluation of performance evaluation of M&A. This has helped us to identify the gaps in existing literature and formulate the objectives for this study. The identified research gaps are provided in the next chapter.