CHAPTER I

INTRODUCTION

The change in the business world throughout the globe is due to the all encompassing phase of economic reforms and liberalization; the combination of national economies with “Market – oriented globalized Economy” being one among the major improvements (Kumar, 2011). A vital part of this new economic pattern is Corporate Restructuring activities such as amalgamations, mergers, consolidation, acquisitions and takeovers (Kaur, 2005).

Reobuck (2012) defines Corporate Restructuring as “The act of reorganizing the legal, ownership, operational or other structures of a company for the purpose of making it more profitable or better organized for its present needs”. Basically, restructuring pose to be a comprehensive reformation conducted for the key purpose of attaining profitability and productivity. Prior to liberalization in India, restrictive government policies and a rigid regulatory structure reduced the scope and means of corporate restructuring activities. Since Globalization, these activities have grown at a faster rate. Merger and Acquisition is a common term used to refer various types of corporate restructuring activities (Vyas, 2008).

Mergers and Acquisitions that happen beyond the boundaries of a country are known as Cross- Border Merger and Acquisition (CBMA). The concept of CBMA evolved in the late 1990’s; United States being the pioneers. In India, the concept came into existence only after the 1991 Liberalization Policy.

Cross Border Merger and Acquisition - Global Scenario

The great merger movement was predominantly a US situation dated between 1895 and 1905; during which nearly 1,800 firms vanished into consolidations (Lamoreaux, 1988). In the late 19th century, business firms concentrated on horizontal mergers that took place between the steel, metal and construction industries. Later in early 20th century, vertical mergers happened. In the third phase (1916 - 1929), Merger and Acquisition process was fueled by the fiscal explosion that took place after the World
War I. Third phase mergers were seen in industries such as metal manufacturers, automobile tools, food products, chemicals, etc. and were basically diversified in nature. This phase saw its closure with a huge decline in stock market followed by the great depression. The fourth phase (1981 - 1989) witnessed acquisitions between bigger firms compared to the earlier phases. The industries active in this phase include banking, pharmaceuticals, oil and gas, and aviation. It ended with the inception of anti-acquisition laws, reorganization of financial institutions and the gulf war. CBMA dominated the fifth phase (1990 - 2000) with the boom in stock market and various deregulation policies towards globalization. Major mergers took place in telecom and banking industry, investments were made through equity transactions. In the sixth phase (2002 - 2008), shareholder activism, private equity and leveraged buyouts strengthened their capabilities in the international market. This timeline observed giant mergers globally in the Telecommunications industry. The seventh phase started from 2011 onwards. The BRICS countries took the vanguard in this phase. Cross- border mergers and industrial consolidations are hoped to flourish.

Considering the cross-border inbound and outbound deal values for the past 25 years (1990 - 2015), the developed economies have contributed more than the developing economies. There are few major noticeable events such as the Gulf War (1990), the Soviet Union collapse (1991), 9/11 World Trade Centre Attack (2001), US Credit Crisis (2007 – 08), and the European Debt Crisis (2010), happened in various parts of the world that had greater impact on CBMA trend. The deal values were highest in 2007, amounting to 1 trillion dollar. Further due to the US credit crisis of 2007 - 08, it started declining. In 2015, the volume and value of cross- border sales and purchases globally has reached to 10044 and 721455 million dollars respectively.

According to the World Investment Report (2016), United States has retained its top position as an investor as well as a host economy among the developed countries in 2015 compared to the previous year rankings. In Asia, China and Japan stand first as a host economy and investor economy respectively. While comparing all the sectors, the service sector has contributed more towards the cross-border deals of the world.
Cross Border Merger and Acquisition - Indian Scenario

The new liberalized policy (1991) of India welcomed international trade, foreign investment, tax reforms, privatization and initiation of inflation controlling measures. These changes and the liberal trade environment led India towards CBMA.

The permissible means of CBMA in India include private placements, joint ventures, financial and technical collaborations, capital markets and preferential allotments. The inbound and outbound deals are approved through RBI (Reserve Bank of India) and the FIPB (Foreign Investment Promotion Board). The prohibited territories include lottery business, gambling and betting, real estate, cigarette and tobacco manufacturing, atomic energy and some activities of railway operations (DIPP, 2016). The Merger and Acquisition set up in India is robustly synchronized by some key legislations namely: The MRTP Act (The Monopolies and Restrictive Trade Practices Act 1969), The FEMA (The Foreign Exchange Management Act 1999), and The Income Tax Act (1961). The Companies Act governs all mergers, acquisitions, amalgamations, de-mergers of business units or divisions of all registered companies. The Takeover Code (1997) takes care of the acquisition of shares in listed Indian companies.

Considering the trend of CBMA in India, starting with less than 5 cross border deals in the year 1991, it has improved to 246 sell out deals (cross border sales) and 124 buy out deals (cross border purchases) in 2014, which is nearly more than 20 times. According to the UNCTAD Report (2014), the value of buy out deals is more than the sell out deals except in the recession phases (2008 and 2011) and their values have increased after 2005 because of 100% Foreign Direct Investment (FDI) acceptance. In India, always FDI and CBMA go hand-in-hand. In the last decade, the volumes of deals were highest in the year 2007 with 223 inbound and 220 outbound. After 2011, the inbound deals had started growing. The shift in focus from outbound to inbound is reasoned out by Grand Thornton in their 2011 deal tracker annual issue. According to the report, trend reversal is led by – “fears over the economic dynamics of the European region and its global impact; and growing domestic market making Indian targets a safer bet”. Revival started in 2013. Since the investiture of the new government in 2014; the new liberalization steps endorsed contributed in attracting FDI from all quarters.
Indian CBMA is well spread throughout the world in diversified sectors. According to the DIPP Report (2016), the top most investors of foreign investment into India are Mauritius (34%) followed by Singapore (16%), and Japan (8%); and the FDI inflows in top 3 sectors include (i) Service (18%), (ii) Construction - development (8%), and (iii) Telecommunication (7%). At present, among Asian countries, India is ranked as the 4th favourable destination for foreign investments (World Investment Report, 2016).

According to Zephyr Merger and Acquisition Portal (2008), the top three host countries of India from 2000 – 2007 are (i) Canada (34%), (ii) USA (24%), (iii) European countries (12%); and the top three sectors with high FDI outflows from 2001 – 2007 include (i) Food and Beverages (19%), (ii) Chemicals (12%), and (iii) Computer Software and Telecom (10%). The choice of host countries has changed after 2008, as Indian companies didn’t want to invest in developed countries which were affected by the US credit crisis. From 2008 -2015 (RBI Database), Singapore (22%), Mauritius (19%), and Netherlands (18%) have become to be the top most destination choices for investment by Indian companies; and the top three sectors include include: (i) Manufacturing (35%); Transport, Storage and Communication Services (21%); Financial, Insurance, Real estate, and B2B Services (17%).

During the 2007 crisis, India had a favorable economic condition which encouraged the industries to go across border to utilize the opportunities that prevailed in the developed countries particularly USA and Europe prior to the crisis. The reports and trend show clearly that there was a noticeable change in the overseas investment in the form of acquisitions. After liberalization more than fifty percent of the Indian acquisitions (986 cross- border acquisitions) were made between 2000 and 2007.

Therefore, this study focuses on the major overseas investments (acquisitions) that took place during the crisis period to understand the financial impact on the acquiring industry as a whole and also analyzed individual firms’ performance after the acquisition. The selected acquisitions pertain to those industries that were the major contributors of FDI outflows.
Statement of the problem

As Cross-border merger and acquisition form a part of any liberalized economy, it is important to understand that the new liberal policy (1991) has caused a positive impact on the Indian economy and its industrial composition.

Cross Border Mergers and Acquisitions are made by the companies to gain the strategic benefits of other countries. Many key aspects have to be addressed when taking these strategic decisions to withstand competition in the global market. These decisions are based on the global environment. Crisis being a component of a global economic cycle, it is necessary for every business firm to learn how to face a crisis situation. The 2007 US financial crisis is termed as one of the biggest in the 21st century; it not only affected USA but also EU and Asia. The effect of the crisis in India was felt only to a meager extent (Prasad and Reddy, 2009). Even then US held its stand as the biggest FDI beneficiary among the developed nations. According to UNCTAD (2009), CBMA buy out in developed countries fell by 33%. Economies of developing countries were indicated as the ones with the greatest investment potential. Therefore, in 2008 strategic investors dominated CBMA activities and India being one among them made aggressive investment to make use of the opportunity. Based on the above discussion, the research questions developed for this study are:

- To check whether the acquisition decision taken by Indian companies during the 2007 crisis period, when there was abundance of opportunity to venture abroad turned out to be successful?
- What are the various macro-economic factors that influenced Indian cross – border acquisitions?
- Is there a financial improvement of the Indian acquirers post acquisition?
- Do the Indian acquirers bring better returns to their shareholders through acquisition announcements?
- Did the employees of the acquirer firms experience any positive change after acquisition?
Need for the study

Therefore, there is a need to study whether the firms that made cross-border acquisition during the US credit crisis has gained from the acquisition. Thus the major cross-border acquisitions made by the Indian companies were analyzed in this study in detail. The competence of the acquisition decision cannot be evaluated in the short-run; hence it focuses on the deals that took place in the past decade.

Considering the existing literature, only few studies have been done in India and also industry comparison was not highlighted. Many researches focused to establish the relationship between the major macro-economic indicators and Foreign Direct Investment, but this study made an attempt to identify the macro-economic factors that influenced Indian cross-border acquisitions and also an attempt is made to find the impact of cross-border acquisitions on the acquirer’s performance. However, research into companies involved in CBMA indicates the higher degree of failure rate and hardly few deals enhanced the shareholders value. Hence, this report throws light on pre and post financial performance of the acquiring companies along with the stock market volatility due to the announcement of the acquisition. The Fortune 500 CFO’s were surveyed and 45 percent ascribed that Merger and Acquisition failure is due to “unexpected post-deal people problem”. Involvement of different cultures intricate the issues related to corporate governance, employee welfare or customer satisfaction. Employees being one of the major stakeholders of any company; hence to check the impact of acquisition on the employees an opinion survey was conducted.

Hence, the current study on “Efficacy of Indian Cross Border Acquisitions” was undertaken with the following objectives.
Objectives of the Study:

1) To identify the macro economic factors that influenced Indian cross-border acquisitions.

2) To compare the pre and post acquisition performance of the selected Indian cross-border acquisitions.

3) To analyze the financial efficiency of the selected firms post - acquisition.

4) To examine the stock price behavior of the selected Indian acquirers.

5) To assess the employee’s perception about the implication of cross border acquisitions.

The key findings of the study will be useful to Indian investors and firms in the industry to make strategic decisions, economic policy makers to stabilize and fine tune the norms related to overseas investments and IT firms to improve working environment for employees post acquisition.
Chapterization

The thesis consists of six chapters. The study overview and conceptual background is given in the introduction, followed by the research gap, objectives and design of the study.

The second chapter (Review of Literature) emphasizes the existing literature relevant for this study. The compiled literature starts with the conceptual overview, global and Indian trends of CBMA followed by the related studies reviewed for this research.

The third chapter (Research Methodology) gives the details regarding the related theories and data (primary and secondary) collected to test the set objectives. Based on the theories and selection of variables, the conceptual framework for this study is explained. It also elucidates the relevant statistical tools and methods used to analyze the secondary data and primary data collected. It is concluded with the limitations of the study.

The fourth chapter (Case Study of Selected Indian Cross-Border Acquisitions) elucidates the 20 cases selected under 5 major sectors (Sector-wise) for this study. Each case is elaborated with all the details related to the deal, starting from the background of the organizations and the deal. The major strategies practiced during the acquisition and the list of notable results and events after acquisition was also discussed.

The fifth chapter (Results and Discussion) is classified into four heads. The first section identifies the macro economic factors that influenced Indian cross border acquisitions. The second sections deals with the Financial Assessment of Cross Border Acquisitions on selected Indian Acquisitions. The third section describes the Stock performance of the selected companies due to Acquisition Announcements and the results were discussed sector wise and also individual company wise. The fourth section reveals the Employee’s Perception regarding the Implication of Cross Border Acquisitions made by the select IT companies.

The major findings of the study along with the summary are given in chapter six (Summary and Conclusion). The key findings are summarized with the relevant suggestions and suitable recommendation followed by the conclusion.