CHAPTER 1
INTRODUCTION

Market for corporate control came into being with the pioneering study of Manne (1965) who introduced mergers and acquisitions (M&As) as a mechanism to improve the inept management of the target company. Since then plethora of research has been conducted in this area with the researchers examining M&As from different perspectives. Two broad hypotheses have been advanced by the researchers to explain the rationale for mergers and acquisitions namely, value maximizing hypotheses and non-value maximizing hypotheses.

The value maximizing hypotheses state that M&As are the positive net present value (NPV) activities that yield positive gains to the shareholders of both the acquiring and the target company as these are driven by the objective of improving the fundamentals of the acquiring company ex post. The value enhancing objectives of the acquiring company are fulfilled when the combined company is able to realize various operating and financial synergies by optimum utilization of physical and financial assets of both companies, remove the managerial inefficiencies at the target company’s end and also when the market power of the combined company improves as a result of the merger and acquisition strategy. While, the non-value maximizing hypotheses state that M&As are negative NPV activities for the acquiring company shareholders as these are motivated by the entrenched managers for their personal benefits or in some other cases these are driven by the overconfident managers, suffering from hubris, for satisfaction of their self esteem. As these acquisitions yield zero economic gains to the acquiring company but pose cost in terms of cost of negotiation, price paid to the target and also pose the potential problems of integration in the post acquisition period hence, these would create overall economic loss for the acquiring company shareholders.

RATIONALE FOR MERGERS AND ACQUISITIONS

The two broad categories of hypotheses proposed to explain the rationale for mergers and acquisitions are detailed as follows:
Value maximizing hypotheses: There are number of acquisition motivations that are consistent with the goal of value maximization, namely synergy, replacement of incompetent management and market power. On the basis of these motivations value maximizing hypotheses can further be divided into following categories:

Synergy hypothesis
Improved management hypothesis
Market power hypothesis

Synergy Hypothesis: Synergy is the additional value that is generated when the combination of two firms results in value creating opportunities for the combined firm that are otherwise not available to these firms operating independently (Damodaran, 2005). In fact, the fundamental rationale behind acquisitions is to combine the specific characteristics of both the firms involved in the acquisitions in such a way that it leads to creation of value through realization of various synergies (Seth, 1990). Synergy exists in an acquisition when the value of combined entity exceeds the sum of value of the combining firms (Bradley et al., 1988), that is, when \( VC > VA + VT \), where \( VC \) refers to the market value of combined firms, \( VA \) refers to the market value of acquiring firm and \( VT \) refers to the market value of target firm. In words of Lubatkin (1983) synergy occurs when two independent companies can be run more efficiently (that is, with lower cost) and also more effectively (that leads to more appropriate allocation of resources with given environmental constraints) together than apart. Various researchers like Mandelkar (1974), Dodd and Ruback (1977), Asquith (1983), Bradley et al. (1983), Schipper and Thompson (1983) who find positive announcement gains for the acquiring and the target company shareholders attribute these gains to the synergies that are realized in terms of increased productive efficiency as a result of the combination of the real assets of the two companies.

Improved management hypothesis: The Improved management hypothesis has its genesis in the pioneering study of Manne (1965) on the market for corporate control wherein he remarks that “mergers are a means of disciplining the inept management”. The hypothesis is further refined and renamed as internal inefficiency hypothesis by Dodd and Ruback (1977). The hypothesis states that if a target company is inefficiently managed,
with the result that the profits are lower than those might be, then the bidding firm is motivated for takeover of such firm so that it can better utilize its resources along with its own resources and can create higher value for the combined firm. The acquiring company desires control of the target firm so as to replace an inefficient management or to force the existing management to follow the value maximization strategies. Thus, mergers are viewed as a response to the sub-optimal policies of the target firm (Asquith, 1983).

Various researchers (Langtieg, 1978; Dodd and Ruback, 1977; Mandelkar; 1974; Asquith et al., 1983; Malatesta, 1983) opine that the positive wealth gains to acquiring and the target shareholders accrue as a result of shifting of the control of an acquired firm’s assets from a relatively inefficient management to superior management of acquiring firm.

*Market power hypothesis:* Market power is the ability of a market participant or group of participants to control the price, the quantity or the nature of the products sold thereby generating extra-normal profits. In related acquisitions, a firm’s market power is increased through horizontal mergers (where the acquiring and acquired firms operate in the same product market) or through product or market related extension acquisition where a firm’s effective size is increased relative to its competitors (Singh and Montgomery, 1988). The dominant firm model of oligopoly again suggests that prices in an industry rise consequent to a horizontal acquisition by a dominant firm. But empirical evidence has not unequivocally ascribed larger gains in mergers and acquisitions to this hypothesis (Eckbo, 1983; Stillman, 1983; Mueller, 1985). Even Jensen and Ruback (1983) who conduct extensive review of extant mergers and acquisitions literature conclude that gains from mergers and acquisitions do not accrue from the creation of the market power.

Thus, the value maximizing hypotheses state that the rationale for mergers and acquisitions on the part of the acquirer is to either take advantage of improved operating and financial efficiencies by combining the physical and financial resources of two companies or to better utilize the target’s resources by redesigning the sub-optimal strategies of target’s managers or else to improve the market share.
Non-value maximizing hypotheses: The non-value maximizing hypotheses can further be divided into following two categories namely size maximization hypothesis and hubris hypothesis.

Size maximization hypothesis: This hypothesis is given by Mueller (1969). It states that in the era of divergence between ownership and control, the managers who have discretionary control over decision making as well as over the free cash flows of the company may use these resources to maximize their personal benefits. Usually, the managers’ personal benefits viz. their salaries, bonuses, perks and promotions are related to the size and growth of the company (Mueller, 1969; Jensen and Ruback, 1983; Faccio and Lasfer, 1999; Morck et al., 1990). If the managers are sufficiently insulated from the objective of shareholder wealth maximization, they may start using the resources of the company for their own benefits rather than pursuing the goal of wealth maximization for the shareholders (for whom they are acting as agents). In this process they start chasing growth by acquiring more and more businesses even those that are completely unrelated to their existing business because they believe that being large may bring prestige and help them in securing their jobs. Thus, driven by this phobia they go on acquiring the businesses, without doing the proper cost benefit analysis, at the cost of shareholders welfare. This is the reason for such acquisitions afflicted by the high private benefit of control generating value losses for shareholders than those acquisitions with no such benefits (Morck et al., 1990). Hence, managerial motivations for a particular acquisition indicate the value creating potential of the merger and acquisition.

Hubris hypothesis: The hypothesis was given by Roll (1986). Hubris refers to an animal like spirit of arrogant pride and self confidence. It states that sometimes the takeovers are motivated by the acquiring company managers who get caught up in believing that they cannot do anything wrong and that their foresight is perfect. Afflicted by this phobia, the acquiring company managers despite the absence of any potential synergistic gains from an acquisition believe such gains to exist and become overconfident about the success of the acquisition. As a result, they end up paying the target company more than its real worth. Such excess premium that is paid without any resultant gain in post acquisition
period results in significant diminution in the wealth for the acquiring company shareholders.

Thus, non-value maximizing hypothesis implies that acquisitions destroy the wealth of the shareholders at large. The reason is that these are either motivated by managers to maximize their personal wealth or are attempts by the acquiring company managers to satisfy their self pride and ego.

The above discussion has put light on the motives behind merger and acquisition moves. It can be concluded that in some cases managers pursue mergers and acquisitions to maximize the wealth of shareholders at large. In such cases managers join hands with the target company only if there are real or financial synergies so that they can improve the fundamentals of the resultant company. While, in other cases managers resort to this route to maximize their personal benefits only or sometimes they are over confident about the success of deal and carry it on without proper valuations.

ROLE OF STRATEGIC BID SPECIFIC AND COMPANY SPECIFIC FACTORS IN IDENTIFYING THE UNDERLYING MOTIVES OF A PARTICULAR ACQUISITION

The pioneering studies that examine the shareholders wealth gains in mergers and acquisitions find that majority of the gains are enjoyed by the target shareholders while the acquiring company either gain or lose or remain at break even. In order to remove the enigma regarding wealth gains to the acquiring company shareholders, the researchers subsequently started analyzing various deal specific and company specific features to examine their influence on the wealth gains. For instance, the researchers like Travlos (1987), Loughran and Vizh (1997), Hansen (1987), Martin (1996), Carleton et al. (1983), Huang and Walkling (1987) highlight the impact of mode of payment on the announcement returns. The researchers like Lewellen (1971), Haugen and Udell (1972), Shelton (1988), Singh and Montgomery (1988) indicate the influence of industry relatedness on the announcement returns of the acquiring company. Further, the researchers like James and Wier (1987), Berkovitch and Narayanan (1990) highlight the influence of competition in takeover market on the acquirer’s announcement returns. Furthermore, the impact of nationality on the wealth gains of the acquiring companies is

These researchers conclude that the reason for the traditional studies presenting conflicting results regarding the acquiring company wealth gains is due to the fact that these studies consider M&As as a homogenous phenomenon and fail to explore the role of the above listed bid related and company specific strategic factors. They opine that in case of information asymmetry between the acquiring managers and the investors at large, these are the factors that act as the indicators of managerial intentions underlying acquisitions and convey a signal about the value enhancing or destroying potential of the acquisitions to the market.

Hence, this section explains the role of the various strategic factors in indicating the value creating potential of an acquisition and in determining the resultant wealth gains to the participating companies. The strategic deal specific variables identified by the researchers are mode of payment employed, industry commonality/relatedness, extent of hostility, competition among the acquirers and the nationality of the target company etc. While, the company specific variable that play key role in determining wealth gains are the absolute size of the acquiring company and the relative size of the target company. The role of all these strategic variables is explained as follows:

**Mode of payment:** In an acquisition the most important decision the acquirer has to take is regarding the price to be paid to the target company that in turn depends upon the value of the assets owned by the target company. However, in a market characterized by information asymmetry, the mode of payment used by the acquirer to satisfy the claims of the target signal the probable risks in the acquisition and the managerial intentions for such acquisition. When the acquirer is not able to assess the true value of the assets at the disposal of the target company, it generally uses the market value of the target’s shares as a proxy of the asset valuation. If the acquirer believes that the target’s shares are
overvalued in the market it will usually finance such acquisition with stock to avoid the risk of adverse selection. The overvaluation of the target’s shares means that the shares of the target company are trading at a premium to the book value of its assets because market expects such companies having huge growth opportunities in future, however, it is difficult to value these opportunities compared to the assets in place (Martin, 1996).

Driven by such overvaluation, the acquirer may overestimate the value of the target company’s resources and as a result it may end up overpaying the target company than its real worth. Besides, it may lead to synergy risk that may make it difficult for the acquirer to actually materialize the synergies that are projected on the basis of market performance and not on the basis of the actual fundamentals of the target company. In order to hedge these two risks the acquirer uses stock to finance these acquisitions due to its contingent pricing effect that is realized in two ways. Firstly, for the same cost to the acquirer it induces the target to accept a stock offer in place of equally costly cash offer (Hansen, 1987). Secondly, it enables the acquirer share the risk of non-performance with that of target shareholders in the post acquisition period through shared ownership.

Furthermore, the acquirer may use stock financing when its own shares are overvalued in the market. It again conveys negative signal to the market that the acquirer itself is skeptic about its own capabilities to attain future growth opportunities by combing the resources of the target company with its own in the post acquisition period.

Thus, the use of stock financing will give negative signal to the market about the bleak prospects of the combined company and also the lack of confidence of the acquirer in the value creating potential of a particular acquisition. On the contrary, a cash acquisition conveys the positive signal about the confidence of an acquirer in correctly assessing the value of a target company that in turn reduces the risk of valuation error and also of losing the expected synergies.

Besides, tax considerations are also the source of higher wealth gains in the cash acquisitions. Cash acquisitions create immediate tax liability for the target company shareholders. Hence, in order to offset the additional tax burden in cash offers the target company shareholders command more premium from the acquiring company. On the other hand, stock offers are tax free transactions because the capital gain tax is deferred until the stock is sold (Davidson and Cheng, 1997). As regard the acquiring company, cash offers
generate higher wealth gains than stock offers as these give the acquiring company the benefits in form of huge depreciation tax shield, interest tax shield that in turn increases the probability of higher cash flows in the post acquisition period (Krishnamurti and Vishwanath, 2008).

Furthermore, the mode of financing also conveys the signal about managerial motivations for an acquisition. Usually, stock financing is employed by the managers who hold insignificant shareholding in the acquiring company and pursue acquisitions just to maximize the size of the acquiring company and to derive personal benefits. The reason being any loss from such a value destroying merger has to be shared by the shareholders at large and not by the managers due to the lesser ownership stakes in their hands. It implies that the probability of a value destroying acquisition increases if the ownership stakes of the managers of the acquiring company are low. However, cash financing is preferred by the managers who hold large percentage of shares in the acquiring company and when they pursue value creating acquisitions as otherwise it will lead to the value destruction of their own shares.

Hence, use of stock financing gives negative signal about the bleak prospects of the combined company and also highlights the negative managerial intentions for an acquisition. Hence, due to these factors the announcement of the stock offers is accompanied with a negative stock market reaction that in turn leads to negative valuation of the acquiring companies’ shares (Kummer and Hoffmeister, 1978; Huang and Walkling, 1987; Travlos, 1987; Sullivan et al., 1994). On the other hand, the cash offers not only highlight the acquirer’s confidence in a particular deal but also conveys the positive managerial intentions. Hence, driven by this positive information, stock markets welcome such acquisitions that in turn lead to positive valuation of share prices of both the target and the acquiring companies (Loughran and Vlah, 1997; Emery and Switzer, 1999; Martynova and Renneboog, 2006).

Thus, mode of payment is a very important factor that influences the wealth gains in an acquisition as it not only conveys the signal of the possible risks in an acquisition but also highlight the managerial intentions underlying a particular acquisition.
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Relatedness: Relatedness in an acquisition indicates the extent of strategic fit achieved in an acquisition and also the resultant sources of synergistic gains (Lubatkin, 1983). A takeover is defined as related when it involves two companies engaged in production of similar products or rendering similar services (case of horizontal mergers) or integration of two companies that are producing same product but are at different stage in the supply chain route (case of vertical mergers) or else includes the joining of two companies that are related through basic technologies, production processes or markets and may represent an extension of the product line or the extension into new markets (congeneric/related mergers). In fact, the universe of related merger includes horizontal mergers, vertical mergers and mergers that represent the movement of a company from its current set of businesses to the adjoining businesses or the extension of the firm from its current market to the newer markets (Chatterjee, 1986). On the other hand, conglomerate/unrelated mergers are those where there is zero commonality between the businesses of the acquiring and the target company either horizontally or vertically.

Generally, related mergers are pursued to obtain various operating synergies as a result of the complementarities between the physical and managerial resources of the two companies. These are realized in the form of economies of scale (leading to the efficiency increase from the expanded production of a specific product), economies of scope (resulting from the use of a given bundle of resources in joint production of two or more products), increased market power and elimination of competition (enabling the acquiring company gain monopoly rents). However, the unrelated mergers are pursued to gain various financial synergies viz. enlarged debt capacity, coinsurance benefit (arising as a result of the diversification into newer areas) and also tax benefits.

Usually, it is presumed that related acquisition strategy would create superior announcement returns to the shareholders than unrelated ones for three reasons. Firstly, the related acquisition besides offering various operating synergies may also yield financial synergies by combining the resources of the two companies. However, the unrelated acquisition can’t duplicate the operating synergies attained in related acquisition except for the managerial synergies. Thus, unrelated acquisitions offer far lesser opportunities to make the combined businesses more defendable (Chatterjee and Lubatkin, 1990). In fact, the related acquisitions are aimed at generating higher future
cash flows for the combined company by optimally utilizing its physical, managerial and financial resources. However, the focus of conglomerate merger is to improve the overall stability of the merged company by optimum utilization of financial recourses.

Secondly, when a company diversifies into its adjoining businesses, the risk of failure is lesser as in such cases the acquiring company is familiar with the modalities of the business and the markets. Thus, potential benefits from related mergers are high because these transactions offer opportunities to diversify around common core of strategic resources (Singh and Montgomery, 1988). On the contrary, due to divergence in the businesses of two companies unrelated mergers can pose various operational risks and also the post merger integration problems. Moreover, when a company diversifies its operations into related areas it is easier for the acquiring company to assess the worth of the target’s resources. Hence, a related acquisition also reduces the risk of valuation error that may be very high in case of unrelated acquisitions (Reuer et al., 2004; Datar et al., 2001). Thirdly, unrelated acquisitions are generally pursued by the entrenched managers who have large cash flows at their disposal but instead of distributing these to the shareholders, managers undertake unrelated acquisitions with a view to maximize the size of the acquiring company and hence their personal benefits.

As a related acquisitions provide signal about the inimitable synergies as also lesser risk of valuation error, lesser post integration problems and further do not convey any signal about the negative intentions of the managers for acquisitions, these may produce superior announcement gains for the acquiring company shareholders. However, researchers possess differing view points with respect to the value creating potential of an acquisition on the basis of relatedness feature (all the studies related to the debate of value creation in related versus unrelated acquisitions has been discussed in the chapter on review of literature).

**Hostility:** The takeovers where the acquiring company tries to gain controlling interest in the target company against the wishes of management and are usually routed through the stock market directly to the shareholders at large are called hostile takeovers. On the other hand, the takeovers that are conducted by the mutual understanding/negotiation between the acquirer and target company’s managers are called friendly takeovers. The
hostility or the attitude of the acquirer again conveys managerial motivations for an acquisition.

If the acquiring company managers are driven by value maximization motive and raise the hostile takeover bid with the objective of replacing the inefficient management at the target company’s end, such acquisitions may create positive wealth for the shareholders at large (Healy et al., 1997). The reason is that in such acquisitions managers would do proper cost benefit analysis and if they feel the price demanded by the target shareholders is exceeding the value of the expected synergies from such acquisitions they would rather abandon it.

However, if the hostile acquisitions are either aimed at deriving personal benefits or are driven by hubris then the managers would pursue these acquisitions at any cost and in the process may end up paying higher premium to the target shareholders. The excessive price premium paid as a result of either of the above two reasons result in substantial gains to the target company but substantial wealth erosion for the acquiring company shareholders (Huang and Walkling, 1987; Georgen and Reneboog, 2004; Dewenter, 1995). Hence, the attitude of the acquirer in an acquisition is an important indicator of the managerial motivations for an acquisition and also signals the distribution of gains among the acquirer and the target shareholders depending upon the extent of price premium paid by the acquirer.

*Competition among acquirers:* Competition hypothesis indicates how the acquisition gains would be distributed between the acquirer and the target company. In fact, the ultimate distribution of the gains between the acquirer and the target depends upon the respective bargaining power of the acquirer among the rival bidders (Capron and Pistre, 2002). This in turn depends upon the resources at the acquirer’s disposal. If the synergy from an acquisition is unique to the target’s assets, it would increase the competition between the acquirer and the rival bidders. This competition among the potential acquirers to win the target company enables the later to fetch a higher price. Usually, the contest among the bidders stretches the price so much that it results in abnormal gains to the target but negative returns to the acquirer (Mandelkar, 1974; Asquith et al., 1983; Dodd and Ruback, 1977; Bradley et al., 1988; James and Wier, 1987). Thus, it is the
competition amongst the bidders that forces them to pass entire gains to target company shareholders by offering them higher prices (Cebenoyan et al., 1992). Hence, in the presence of a competitive acquisition market, the acquirer would gain only if the source of synergy is unique to the resources at the disposal of the acquirer itself or else if the acquirer and the target present a unique combination of resources (Asquith et al., 1983) otherwise the acquirer has to transfer entire gains to the target in form of higher acquisition price.

**Nationality:** Nationality is also an important factor that highlights the sources of gains for an acquirer. It is presumed that an acquirer gains superior returns in cross border acquisition compared to those of domestic acquisitions because cross border acquisitions besides conferring the general benefits of an acquisition like economies of scale, economies of scope and increased market power also enable an acquiring company take advantage of frictions in capital/financial, factor and forex markets. Three competing theories namely international diversification theory, internalization theory and exchange rate theory have been offered as the drivers of value creation in cross border acquisitions by the researcher. The advocators of international diversification theory state that the cross border acquisition enables an acquiring company earn abnormal gains as it offers the acquirer opportunities to diversify the risk across geographies taking advantage of imperfections in financial markets. Similarly, researchers advocating internalization theory state that shareholders earn abnormal returns in these acquisitions as these offer an opportunity to create an internal market for the judicious use of intangible and indivisible resources and capabilities of the combined company (Magee, 1981; Buckley and Casson, 1998; Morck and Yeung, 1991; Makides and Ittner, 1994; Harris and Ravenscraft, 1991). Lastly, the supporters of exchange rate hypothesis opine that abnormal returns in cross border acquisitions are attributed to the frictions in the exchange rate markets that enable the acquirer to acquire valuable resources of the target company at affordable prices. Due to these additional benefits cross border acquisitions create higher returns than the domestic acquisitions.

**Size of the acquiring company:** Size of the acquiring company itself is also an important factor affecting wealth creation in acquisitions. It has been suggested by the researchers
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(Mandelkar, 1974; Roman and Michael, 2006) that the larger acquiring companies make value destroying mergers as the managers of such companies are more prone to hubris and also pursue acquisitions for their personal benefits. Accordingly, researchers find a negative relation between the size of the acquiring company and the wealth gains of its shareholders.

Relative size of the target company: The relative size of the target company is also an important determinant of wealth gains as it reflects the possible risk associated with the realization of synergies in the post acquisition period. Two diverse view points prevail with regard to the role of size of the target company in influencing the wealth gains in mergers and acquisitions. At one extreme researchers like Kusewitt (1985), Danbolt (2004) and Hansen (1987) opine that acquiring a relatively larger target company increases the risk of performance in the post acquisition period and tend to be a case of biting off more than one can chew. The reason being the acquisition of a target company larger than the relative size of the acquirer poses various managerial problems viz. problems in integrating the operations in the post acquisition period and also creates financial problems as the acquiring company generally has to raise debt to finance an acquisition larger than its own size.

On the other hand, the researchers like Seth et al. (2002) and Shelton (1988) state that acquiring larger target company is favorable as it offers exceptionally valuable assets and opportunities to the acquiring company such as national brand names and distribution system, increased market power, enlarged economies of scale and economies of scope. Thus, the role of relative size of the target company in explaining the wealth gains is ambiguous.

Thus, from the above discussion it is clear that the strategic bid related and company related factors play prominent role in highlighting the motives for a particular acquisition and its resultant influence on the target and acquiring company shareholder wealth. Though, there are various drivers for merger and acquisition activity but the presence or the absence of a particular driver is highlighted through the features of deal and of the participating companies itself. It is only after exploring these factors the positive and negative motivations of the acquiring company managers, the sources of
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gains and the distributions of these gains between participating companies can be understood.

CONTEMPORARY STRATEGIC ISSUES IN MERGERS AND ACQUISITIONS

Mergers and acquisitions is an ever evolving area where new phenomena are tried by the practitioners and their impact on the wealth gains are assessed by the researchers. Two strategic issues that have emerged in this area recently are the concept of earnout mergers and that of brand acquisitions. These strategic issues and their influence on the shareholders wealth gains are detailed as follows:

Earnout acquisitions: In addition to the cash and stock offers that are commonly used by the acquiring companies to satisfy the claims of the target shareholders, an alternative mode of payment employed by the acquirer for managing the problem of valuation error and that of adverse selection is earnout (Hansen, 1987; Kohers and Ang, 2000; Datar et al., 2001; Reuer et al., 2004; Cain et al., 2006). An earnout is a contractual agreement in which the acquiring company makes payment to the target in two or more parts, that is, an up front payment which is made at the time of entering into the contract and a deferred payment or an earnout that is linked to the attainment of pre-specified performance targets within a pre-specified time period by the target company. The amount of up front payment reflects the mutually agreed upon portion of transaction value while earnout reflects the extent of disagreement between the target company and the acquiring company (Kohers and Ang, 2000).

An earnout offer enables an acquiring company to share the risk of overpayment ex post with the target company by making the part payment contingent upon future performance benchmarks. By linking the part payment to the future performance targets it also reflects the inherent strengths of the target company because only that target company which believes in its potential to create value in the post acquisition period would accept such an offer where part payment is premised on its ex post performance.

Another reason for employing earnout offer is that it serves as a tool to retain the managers of the target company who may possess the expertise and the specific knowledge in relation to the operations of the target company that can otherwise not be
duplicated (Kohers and Ang, 2000). By retaining the target managers and linking their earnings to their future performance, earnouts try to align the managerial objectives with organizational objectives. This in turn resolves the agency problem as highlighted by Reeb et al. (1998) that arises due to the difficulty faced by an acquiring company in overseeing the actions of managers.

Hence, earnout offers, by resolving the problem of adverse selection on the one hand and by acting as a tool to retain the managers of the target company on the other hand enable the acquiring company in attaining the pre-specified performance targets through the target company itself and consequently help in mitigating the probable risks involved in realizing the expected synergies in the post acquisition period. Thus, a positive relation is expected between an offer being financed with an earnout mechanism and the announcement gains of the acquiring and the target company.

Brand acquisitions: Resource based view states that the source of competitive advantage for a company lies in it possessing superior resources along with superior skills to mobilize these resources (Doyle, 2001; Thompson and Strickland, 2001). Brands are one such resource that has become important for companies as these are the strategic assets that drive core business processes and enables a company to create competitive advantage in the market place (Biel, 1997; Urde, 1999; Doyle, 2001). Brands are an important determinant of the shareholder wealth as these provide opportunity to enhance the future cash flows by improving market performance and market efficiency, on the one hand; and by reducing the risk associated with non-realization of cash flows by creating long term relational network with the customer, on the other.

Brands can be built in-house; else these can be acquired from another company either indirectly while acquiring the control of a company or directly in a stand alone brand acquisition transaction. However, building a brand from a scratch is expensive as it requires huge investment, has long gestation period coupled with a lower probability of success. Moreover, in a market characterized by highly dynamic business environment where resources erode very quickly, it would be risky for a company to lose time in experimenting products with new brand names in the market. Hence, in such a dynamic environment, the company’s quest for competitive advantage through strategically
valuable resources and capabilities can be fulfilled by acquiring these resources (brands) from another company via acquisitions. Since brand acquisitions are aimed at filling the existing resource gap influencing the future performance of a company, hence a positive relation is expected between the brand acquisitions and their impact on shareholders wealth.

As the upshot of the above discussion it is clear that the merger and acquisition activity is initiated by the acquiring company managers either for maximizing the wealth of shareholders at large or these are driven by the personal objectives of the managers. However, to get insight into the value creating potential of the acquisition, there is a need to explore the influence of various bid related and company related factors. The reason is that in case of information asymmetry between the acquiring company and the investors, analysis of these factors signify the sources of the gains in an acquisition, the managerial intentions for an acquisition that in turn signal the direction in which the acquisition gains will flow that is, whether these will be enjoyed by the acquirer or the target solely or else shared between the acquirer and the target. This not only resolve the ambiguity regarding the acquisition wealth gains to the acquiring company but also give insight into the reasons that cause entire acquisition gains to be shifted to the target shareholders.

Moreover there is a need to explore the role of contemporary issues like earnouts that have been designed to tackle the problem of adverse selection on part of the acquirer and that of brand acquisitions that are undertaken to fill the intangible resource gap by an acquiring company in a dynamic environment.

**NEED FOR THE STUDY**

Though a plethora of research has been conducted on mergers and acquisitions and its impact on shareholders wealth gains internationally. However, in India very few researchers have examined the impact of mergers and acquisitions on the shareholders wealth in domestic and cross border acquisitions. Beena (2000) has studied the impact of mergers and acquisitions on the share prices of the acquiring company while Pandey (2001) has examined the target shareholder wealth gains in open offers. Further, Mishra and Goel (2005) have studied the impact of a single acquisition between Reliance India Limited and Reliance Petroleum Limited on the announcement returns of the acquiring
and the target company shareholders. Anand and Singh (2008) examine the impact of
bank mergers on the acquiring and the target shareholders wealth gains.

As regard the assessment of wealth gains in cross border acquisitions, Zhu and
Malhotra (2008) analyze the impact of such acquisitions on the acquiring company
wealth gains but restricted the sample to only the US targets. Further, there are some
theoretical studies that analyze the patterns and motivations of cross border acquisitions
by Indian acquirers (Pradhan and Abraham, 2003; Mathew and Jain, 2006). Thus, there
is no study that has comprehensively analyzed the impact of either domestic or cross
border acquisitions on the wealth of the acquiring and the target company shareholders.

Moreover, the strategic issues like earnouts and brand acquisitions are prevalent
in India but no research has been conducted on assessing the impact of these issues on the
shareholders wealth gains. Thus, there is a need of a comprehensive study that unearths
the impact of all the above issues on the wealth of the acquiring and target company
shareholders in the Indian context. Thus, this study attempts to fill the void in the existing
mergers and acquisitions literature by analyzing the announcement gains of the acquiring
and the target companies in domestic and cross border acquisitions as well as attempts to
examine the impact of the strategic factors on the shareholders announcement returns.

**OBJECTIVES OF THE STUDY**

The specific objectives of the study are detailed as follows:

1. To examine the impact of mode of payment on the acquiring and target
shareholder announcement returns in domestic acquisitions.
2. To examine the impact of insider ownership on the acquiring and target
shareholder announcement returns in domestic acquisitions.
3. To assess and compare the target company’s announcement returns in inbound
cross border acquisitions and domestic acquisitions
4. To evaluate and compare the acquiring company’s announcement returns in
outbound cross border acquisitions and domestic acquisitions
5. To study the impact of earnout acquisitions on the announcement returns of the
acquiring companies.
6. To examine the impact of brand acquisitions on the announcement returns of the acquiring companies.

**ORGANIZATION OF THE STUDY**

The study is divided into eight chapters. The first chapter, that is, the present chapter gives introduction of the topic elaborating the rationale for mergers and acquisitions and the role of various bid specific and company specific strategic factors in influencing value creation in mergers and acquisitions. It also explains the need and the objectives of the study.

The second chapter reviews the extant literature on mergers and acquisitions. It has been divided into four categories. Firstly, the review on various studies giving the rationale for mergers and acquisitions has been detailed. Secondly, the studies showing the role of strategic bid related and company specific factors on the acquiring and the target company shareholder wealth have been explained. Thirdly, the studies related to various contemporary issues in mergers and acquisitions that is, studies related to earnout offers and brand acquisitions have been discussed. Lastly, the studies relating to Indian mergers and acquisitions have been explained.

Third chapter details the research methodology. It defines the scope of the study that is the research question defining the aim of the study; the period for which the study has been conducted; sources from where data has been collected; description of the sample set and details of different statistical tools & techniques used for the data analysis.

Chapter four to eight relates to analysis and interpretation on different objectives being set in the study.

Fourth chapter presents the analysis and interpretation on the impact of mode of payment and ownership structure on the announcement gains of the acquiring and the target company shareholders.

Fifth chapter presents the analysis and interpretation on the impact of outbound and inbound cross border acquisitions on the announcement gains of the acquiring and the target company shareholders respectively.

Sixth chapter analyzes the likelihood of the earnout offers and also study the effect of earnout offers on the acquiring company shareholders’ wealth gains.
Seventh chapter analyzes the impact of brand acquisitions on the announcement returns of the acquiring company shareholders.

The final chapter that is, the eighth chapter presents summary and conclusions of the study and winds up with the recommendations for the managers, the market regulator SEBI, the promoters and the financial institutions.