Impact of Acquisition on Performance of Indian Companies – A Comparative Study of Domestic and Cross Border Acquisitions

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Abstract

Mergers and acquisitions (M&As) are key corporate strategy actions that are vital for the companies in order to survive in this competitive global world. Over the years, the popularity of those actions has increased, especially in the international domain. In India, both the number and value of cross-border M&As has increased significantly over the years. Despite this increase, there haven't been enough studies or clear evidence about whether venturing abroad to acquire foreign targets leads the companies to better performance compared to staying domestically. The purpose of this paper is to investigate the M&A phenomenon deeply and compare between cross-border and domestic M&As made by Indian firms. The broad objective of this paper is to measure the impact of M&As on the financial indicators of acquiring Indian firms.

Key words: Mergers and acquisitions, Cross-border acquisitions, Financial performance, India.

Introduction

Corporate rebuilding has turn into a noteworthy segment in the budgetary and financial environment everywhere throughout the world. Modern restructurings have raised vital issues for business choices and in addition for open detailing approach. Since 1991, Indian commercial enterprises have been progressively presented to both local and worldwide rivalry and intensity. Subsequently, as of late organizations have begun rebuilding their operations around their center business exercises through mergers and acquisitions. In recent years, M&As are increasingly getting accepted by Indian businesses as a critical ingredient to achieve strategic growth by building global footprint. Historically, the strategy of M&As is being adopted to access the market through an established brand, to reduce competition, to increase market share, to acquire competence or to reduce tax liabilities or to adjust accumulated losses of one entity against the profits of other entity (Rani, et 2014). In recent times, there has been a substantial growth in Cross-border acquisitions, with India being one of the major emerging market acquirer in the global market.

Literature Review

The past studies on M&As have focused on varied objectives. One objective has been to study the determinants of acquisitions (Haleblian, et al, 2009; Trahan, 1993; Huyghebaert, et al, 2010). On Indian front, Kumar (2007) and Pradhan, et al (2004) have analyzed M&As and Cross-border acquisitions to identify the determinants.
Another objective has been to study the impact of M&As on the performance of the acquiring firm. In the field, despite having extensive literature on the value creation/destruction of mergers and acquisitions, the empirical evidence on returns to acquirer' shareholders does not converge to any conclusion. Many studies have found that there has been significantly negative return in the range of one to five percent prior to announcement to shareholders of the acquiring firms (Datta & Puia, 1995; Sirower, 1997; Corhay & Rad, 2000; Walker, 2000; DeLong, 2001; Houston et al., 2001; Doukas et al., 2002; Goergen & Renneboog, 2004; Beitel et al., 2004). On the other hand, many studies (Markides & Ittner, 1994; Schwert, 1996; Eckbo & Thorburn, 2000; Kohers & Kohers, 2000; Kiymaz, 2003) observe positive return. Some of the studies find significant positive abnormal returns for acquiring firms (upto seven per cent) around the

announcement. Bruner (2002) suggested in a review paper that these varied results make the conclusions regarding the acquirer firms' performance more difficult.

The same phenomenon is also observed for domestic acquisitions, Moeller et al. (2005); Lowinski et al. (2004); and Conn et al. (2005) find positive average return for domestic acquisitions; while, Jarrell et al. (1988); Jarrell & Poulsen (1989); Mulherin and Boone (2000); Andrade et al. (2001); Bruner (2005) find no gains for acquirers in domestic acquisitions.

As far as cross-border acquisitions, Markides and Ittner (1994) document positive return and Eun et al. (1996) also report that cross-border acquisitions increase wealth for target as well as acquiring firms.

On the other side, many studies have documented no significant gains for cross-border acquitions (Doukas & Travlos, 1988; Uddin & Boateng, 2009; Basu & Chevrier, 2011). In summary, the evidence on the wealth effects of cross-border acquisitions for acquiring shareholders is inconclusive. There have been many studies conducted to compare the implications of domestic versus cross border acquisitions for acquirers (Cakici et al., 1996; and Francis et al., 2008) which provide empirical evidence for higher stock returns on domestic acquisitions relative to cross-border acquisitions of US acquirers. On the other hand, Campa and Hernando (2004) document lower return for acquirers acquiring targets in different countries in Continental European. Eckbo and Thoburn (2000) also find better announcement returns for domestic firms relative to cross-border firms in Canada. Mangold and Lippok (2008) suggest that cross-border acquisitions generate significant negative returns while domestic acquisitions create value for shareholders of German acquirers. Lowinski et al. (2004) observe no difference in the returns of domestic and cross-border acquisitions to Swiss acquiring firms. They analyze the performance of 114 domestic and cross-border acquisitions by Swiss acquirers during the period from 1990 to 2001.

In marked contrast to the above empirical findings reporting higher returns to acquirers for domestic acquisitions relative to cross-border acquisitions, Kang (1993) observes higher gains for Japanese acquirers targeting acquisitions in US compared to domestic acquirers there.

In recent works, Zhu and Malhotra (2008); Gubbi et al. (2010); Barai and Mohanty (2010); Kohli and Mann (2011); Rani et al., (2012) observe positive returns for cross-border acquisitions by Indian acquirers. Kose et al., (2010); Zhu (2011); and Zhu et al., (2011) document positive returns for the acquirers from emerging economies. Kashiramka and Rao (2013) studied the shareholders wealth effect of M&As and found that both the acquiring firms and target firm shareholders gained on acquisition announcement irrespective of the period of announcement of the deal, but mergers on the other hand generate wealth losses for the acquiring firms across all periods. Keeping in mind that the studies have not studied financial impacts on a comparative mode, the present study is focused on understanding the impact of M&As, including cross-border, on the financial health of the acquiring firms based in India.

Objective

The broad objective of this study is to measure the impact of mergers and acquisitions on financial indicators in Indian firms. The broad objectives are as follows:

1. To examine and evaluate the impact of mergers and acquisitions on the liquidity and leverage position of the selected units by some important parameters of liquidity and leverage management
2. To examine and evaluate the impact of mergers and acquisitions on the profitability position of the selected companies by some important parameters of profitability management

Sample and Data Collection

The study has been done on the micro-level, as it is not possible to conduct it on the full macro level. The population of the study consists of all types of the companies having different operations of business and totally different nature of industries. As such the universe of the study is Indian companies; the study is based on 8 organizations, which have acquired domestics and foreign companies during 2000-2010 period. The study is not focused on any specific acquisition.

Domestic Acquisitions
1. Reliance Industries Ltd.
2. Tata Chemical Ltd.
3. Tata Steel Ltd.
4. Zee Entertainment Enterprises Ltd.

Cross Border Acquisition
1. Hindalco Industries
2. United Brewries Ltd.
3. Tata Steel Ltd.
4. Tata Motors

The study is based on the secondary data taken from the published sources like annual reports and other similar databases.

Tools for Analysis

The present study is mainly intended to examine the financial performance of merged companies five years before merger and five years after merger by focusing on various financial performance indicators. The tools used are descriptive analysis and hypothesis testing using t-test for dependent samples.

DATA ANALYSIS

I. LIQUIDITY AND LEVERAGE RATIO

Return on Capital Employed

Domestic Acquisitions

	Return on Capital Employed	
	Before	**After**
Reliance	11.48	10.44
Tata Chemicals	11.34	15.73
Tata Steel	7.52	6.81
Zee Entertainment	14.95	5.48
t-test	0.594846414	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
5% level of significance table value = 3.182; thus the Null Hypothesis is accepted.

Cross Border Acquisition

	Return on Capital Employed	
	Before	**After**
Hindalco	15.2	8.9
Tata Steel	12.1	13.06
Tata Motors	20.51	10.26
UB	1.23	7.4
t-test	0.641824	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: For domestic acquisitions, ROCE was the highest in ZEE Co. at 14.95% and the lowest in TATA STEEL at 7.52% before mergers and acquisitions. After M&A, it was the highest in Tata Chemical Ltd. at 15.73% and the ZEE at 4.48%. After mergers and acquisitions, the financial performance of selected units decreased except Tata Chemical Ltd. The result shown by 't' test reveals that the difference in return on gross capital employed is ***not significant*** in the selected units, before and after mergers and acquisitions.
In case of cross border acquisition, ROCE was the highest in TATA Motors at 20.51% and the lowest in UNITED BREWERIES at 1.23% before mergers and acquisitions. After M&A, it was the highest in Tata STEEL at 10.26% and lowest for UB at 7.4%. After M&A, the financial performance of selected units was decreased except Tata Steel Ltd. The result shown by 't' test reveals that the difference in return on gross capital employed is ***not significant*** before and after mergers and acquisitions.

Return on Net Worth

Domestic Acquisitions

	Return on Net Worth	
	Before	**After**
Reliance	11.48	12.49
Tata Chemicals	13.68	18.05
Tata Steel	9.16	8.09
Zee Entertainment	21.63	6.44
t test	0.631811955	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the null hypothesis is accepted.

Cross-border Acquisition

	Return on Net Worth	
	Before	**After**
Hindalco	14.97	7.19
Tata Steel	11.32	13.45
Tata Motors	11.97	6.32
UB	-24.99	2.79
t-test	0.50434	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the null hypothesis is accepted.

Findings: RONW was the highest in TATA CHEMICAL Co. at 13.68% and the lowest in TATA STEEL at 9.16% before mergers and acquisitions. After M&A it was the highest in Tata Steel at 18.05% and ZEE at 6.14%. After mergers and acquisitions, the financial performance of selected units decreased except Tata Steel Ltd. The result shown by 't' test reveals that the difference in return on gross capital employed is ***not significant*** before and after mergers and acquisitions.

In case of cross border acquisition, RONW was the highest in HINDALCO at 14.97% and the lowest in UNITED BREWERIES at 1.23% before mergers and acquisitions. After M&A it was the highest in Tata STEEL at 13.45% and lowest in UB at 2.79%. After mergers and acquisitions the financial performance of selected units was decreased except Tata Steel Ltd. The result shown by 't' test reveals that the difference in return on gross capital employed is ***not significant*** before and after mergers and acquisitions.

<u>Return on Long Term Funds</u>

Domestic Acquisitions

	Return on Long term Funds	
	Before	**After**
Reliance	13.9	17.13
Tata Chemicals	9.29	18.32
Tata Steel	11.3	11.59
Zee Entertainment	37.17	6.54
t test	0.508397	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Return on Long term Funds	
	Before	**After**
Hindalco	15.44	9.44
Tata Steel	12.67	13.06
Tata Motors	21.03	11.39
UB	1.26	9.07
t-test	0.485347	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: ROLTF was the highest in ZEEL Co. at 37.17% and the lowest in Tata Chemical at 9.91% before mergers and acquisitions while after mergers and acquisitions it was the highest in TATA CHEMICAL at 18.32% and the lowest in ZEE at 6.54%. The result shown by 't' test reveals that the difference in return on long term funds is ***not significant*** before and after mergers and acquisitions.
In case of cross border acquisition, this ratio was the highest in TATA MOTORS at 21.03% and the lowest in UNITED BREWERIES at 1.26% before mergers and acquisitions. After M&A it was the highest in Tata STEEL at 13.06% and lowest in UB at 9.07%. The result shown by 't' test reveals that the difference in return on long term funds is ***not significant*** before and after mergers and acquisitions.

Earnings Per Share

Domestic Acquisitions

	Earnings per Share	
	Before	**After**
Reliance	20.26	52.26
Tata Chemicals	8.83	13.49
Tata Steel	11.03	11.68
Zee Entertainment	18.72	3.5
t-test	0.56271	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Earnings per Share	
	Before	**After**
Hindalco	92.12	11.69
Tata Steel	15.05	71.58
Tata Motors	9.38	0.95
UB	-10.97	1.14
t-test	0.177068	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Mm,……… …The EPS was highest in Reliance at Rs. 20.26 and the lowest in TATA STEEL at Rs.8.83. After M&As, EPS increased for all firms except ZEE. The result shown by 't' test reveals that the difference in EPS is ***not significant*** before and after mergers and acquisitions.
In case of cross border acquisition, EPS was highest in HINDALCO at Rs.92.12 and the lowest in UNITED BREWERIES at Rs. 10.92 before mergers and acquisitions. After M&A, it was the highest in Tata STEEL at Rs. 71.58 and lowest TATA MOTOR at Rs. 0.95. The result shown by 't' test reveals that the difference in EPS is ***not significant*** before and after mergers and acquisitions.

Current Ratio

Domestic Acquisition

	Current Ratio	
	Before	**After**
Reliance	1.74	1.37
Tata Chemicals	0.92	1.06
Tata Steel	1.71	1.03
Zee Entertainment	3.36	3.58
t-test	0.807013	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Current Ratio	
	Before	**After**
Hindalco	1.76	0.96
Tata Steel	0.84	1.12
Tata Motors	0.8	0.5
UB	3.22	1.85
t-test	1.555698	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: This ratio was the highest in ZEEL at 3.36:1 and the lowest in Tata Chemical Ltd. at 0.92:1 before mergers and acquisitions while after mergers and acquisition, it was the highest in ZEEL at 3.58:1 and the lowest in Tata Steel Ltd. at.03:1. After mergers and acquisitions the current ratio was decreased except ZEEL and Tata Chemical Ltd. The result shown by 't' test reveals that the difference in current ratio is ***not significant***, before and after mergers and acquisitions.
In case of cross border acquisition, This ratio was the highest in UB at 3.22:1 and the lowest in Tata MOTORS at 0.8:1 before mergers and acquisitions while after mergers and acquisitions it was highest in UB at 1.85:1 and the lowest in Tata MOTOR at 0.5:1. The result shown by 't' test reveals that the difference in current ratio is ***not significant***, before and after mergers and acquisitions.

<u>Quick Ratio</u>

Domestic Acquisition

	Quick Ratio	
	Before	**After**
Reliance	1.33	0.87
Tata Chemicals	1.01	1.24
Tata Steel	1.13	0.68
Zee Entertainment	2.99	3.04
t-test	0.896621	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Quick Ratio	
	Before	**After**
Hindalco	1.6	0.34
Tata Steel	0.78	0.76
Tata Motors	0.52	0.43
UB	4.15	2.85
t-test	1.885541	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: Quick or liquid ratio was the highest in ZEEL at 2.99:1 and the lowest in TATA CHEMICAL at 1.01:1 before mergers and acquisitions. It was the highest in ZEEL at 3.04:1 and the lowest in Tata Steel Ltd. at 0.68:1 after mergers and acquisitions. This ratio showed the mixed trend in selected 4 units after mergers and acquisitions. After M&As, Quick Ratio decreased in 2 units (Tata Steel Ltd. and Reliance Ltd.) and increased in 2 units (ZEEL Co. Tata Chemical Ltd.). The result shown by 't' test reveals that the difference in Quick ratio is ***not significant***, before and after mergers and acquisitions.
In case of cross border acquisition, Quick or liquid ratio was the highest in UB at 4.15:1 and the lowest in TATA MOTOR at 0.052:1 before mergers and acquisitions. It was the highest in UB at 2.85:1 and the lowest in Hindalco at 0.34:1 post mergers and acquisitions. This ratio showed the decreased in quick ratios of all selected units. The result shown by 't' test reveals that the difference in Quick ratio is ***not significant***, before and after mergers and acquisitions.

II. PROFITABILITY RATIO

<u>Gross Profit Ratio</u>

Domestic Acquisition

	Gross Profit Ratio	
	Before	**After**
Reliance	14.07	12.75
Tata Chemicals	23.88	32.45
Tata Steel	14.86	13.87
Zee Entertainment	32.32	37.07
t-test	1.15269	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Gross Profit Ratio	
	Before	**After**
Hindalco	44.26	12.08
Tata Steel	19.79	31.36
Tata Motors	7.7	4.73
UB	-17.87	39.62
t-test	0.45336	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: This ratio was the highest in ZEEL Co. at 32.32% and the lowest in RELIANCE at 14.07% before mergers and acquisitions while after mergers and acquisitions it was the highest in ZEEL Ltd. at 37.07% and the lowest TATA Steel at 13.67%. The result shown by paired't' test reveals that the difference in return on gross profit ratio is ***not significant***, before and after mergers and acquisitions. The profitability of selected units is not improved after mergers and acquisitions.
In case of cross border acquisition, this ratio was the highest in HINDALCO at 44.26% and the lowest in UB at 17.87% before mergers and acquisitions while after mergers and acquisitions it was the highest in UB at 39.62% and the lowest in TATA MOTOR at 4.73%. The result shown by 't' test reveals that the difference in return on gross profit ratio is ***not significant***, before and after mergers and acquisitions. The profitability of selected units is not improved after mergers and acquisitions.

Net Profit Ratio

Domestic Acquisition

	Net Profit Ratio	
	Before	**After**
Reliance	11.53	10.32
Tata Chemicals	10.51	13.62
Tata Steel	7.44	6.83
Zee Entertainment	28.75	28.02
t-test	0.14022	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Net Profit Ratio	
	Before	**After**
Hindalco	27.66	8.83
Tata Steel	8	19.96
Tata Motors	3.29	2.26
UB	-21.3	8.19
t-test	0.52846	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: This ratio was the highest in ZEEL Co. at 28.75% and the lowest in TATA STEEL at 7.44% before mergers and acquisitions while after mergers and acquisitions it was the highest in ZEEL Ltd. at 28.02% and the lowest in TATA STEEL at 6.53%. After mergers and acquisitions the financial performance of selected units declined. The result shown by 't' test reveals that the difference in return on net profit ratio is ***not significant*** before and after mergers and acquisitions.
In case of cross border acquisition, This ratio was the highest in Hindalco at 27.66% and the lowest in UB at -21.3% before mergers and acquisitions while after mergers and acquisitions it was the highest in TATA STEEL at 19.96% and the lowest in TATA MOTOR at 2.26%. After mergers and acquisitions the financial performance of selected units declined. The result shown by 't' test reveals that the difference in return on net profit ratio is ***not significant***, before and after mergers and acquisitions.

<u>Operating Profit Ratio</u>

Domestic Acquisition

	Operating Profit Ratio	
	Before	**After**
Reliance	20.58	18.4
Tata Chemicals	27.84	36.38
Tata Steel	20.5	20.93
Zee Entertainment	33.06	38.48
t-test	1.26409	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Cross Border Acquisition

	Operating Profit Ratio	
	Before	**After**
Hindalco	42.74	14.98
Tata Steel	25.86	35.7
Tata Motors	11.17	7.69
UB	-4.44	41.66
t-test	0.40053	

H0 = There would be no significant difference in means score of ratio in selected units, before and after M&A.
Based on t-test, the Null Hypothesis is accepted.

Findings: The operating profit ratio was the highest in ZEEL at 33.06% and the lowest in TATA STEEL at 20.50% before mergers and acquisitions. After mergers and acquisitions it was the highest in ZEEL at 38.48% the lowest in Reliance at 18.4%.The result shown by't' test reveals that the difference in operating profit is ***not significant***, before and after mergers and acquisitions. After mergers and acquisitions, the operating profit ratio did not improve in selected units.
In case of cross border acquisition, The operating profit ratio was the highest in Hindalco at 42.74% and the lowest in UB at -4.44% before mergers and acquisitions. After mergers and acquisitions it was the highest in UB at 41.66% and lowest in TATA MOTORS at 7.69%.The result shown by 't' test reveals that the difference in operating profit is ***not significant***, before and after mergers and acquisitions. After mergers and acquisitions, the operating profit ratio had mixed results in selected companies.

Conclusion

In the era of growing cross border mergers and acquisitions to expand the presence across globe, the firms at times lose focus on the outcome of these strategies. The impact on financial performance indicators does not provide a valid reason for engaging in cross border acquisitions. This paper attempts to examine the impact on the financial performance of various Indian acquirer companies engaged in cross-border acquisitions and domestic acquisitions during the period 2000 to 2010. The study documents that the impact of M&As on the financial performance of the acquirer firms is not significant on all parameters – leverage, liquidity and profitability. Based on findings, the management of the acquirer firm should remember the fact that although the M&As are focused on gaining strategic advantage, these strategies may not result in having financial advantages at least in the short to medium term.

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