GLOBAL ACADEMIC RESEARCH INSTITUTE

COLOMBO, SRI LANKA

International Journal of Accounting, Finance and Economics

ISSN 2659-2185

Volume: 01 | Issue: 02

On 15th May 2019

http://www.research.lk

Author: Dr. Kandarp Chavda

JG College of Commerce

GARI Publisher | Commerce | Volume: 01 | Issue: 02

Article ID: IN/GARI/IJAFE/2019/112 | Pages: 09-15 (07)

ISSN 2659-2185 | Edit: GARI Editorial Team

Received: 02.03.2019 | Publish: 15.05.2019

AN IMPACT OF MERGER AND ACQUISITION ON FINANCIAL PERFORMANCE OF SELECTED FINANCIAL SERVICE COMPANIES

Dr. Kandarp Chavda
JG College of Commerce, Ahmedabad
kandarp_chavda@yahoo.com

ABSTRACT

Most of the companies all over the world opt for Merger or Acquisition as strategy for their business enlargement. Whenever any merger or acquisition is announced, all the newspapers, media, news channels publish an article or telecast the news on the advantages and disadvantages of the merger or acquisition deal. But it is hard to find any noteworthy articles or news about the actual advantages and disadvantages received or faced by the acquirer company as well as by the target company. Recently, when Vijaya Bank, Dena bank and Bank of Baroda joined hands together, one nice thought spoken in the advertisement is that "Together we are, make us better to best". Which is exactly the meaning and terminology of two plus two is equal to five for Merger and Acquisition. But is the acquisition deal really successful for an acquirer, or the shareholders of the acquirer or anyone who is directly or indirectly connected with this deal? It is hard to find a single significant article after a period of a year in a newspaper on answering this question. This paper is specially made to check the impact of merger and acquisition on financial performance of financial service companies.

Keywords: Merger, Acquisition, DuPont analysis, Financial Performance, Paired t-test.

INTRODUCTION

Liberalisation and Globalisation aspects of economic reforms 1991 have opened up a whole for lot of challenges both in the domestic and international spheres. The increased competition in the global market has prompted the Indian companies to go for mergers and acquisitions as an important strategic choice as well as international players to come into the emerging Indian industry to find massive customers. This led to structural changes caused by the increased competitive pressure in Indian industry. As a result multinational companies were thought to come in India for their business expansion.

The merger and acquisition has become very famous way business expansion in today's fast growing economy. In India, the concept of merger and acquisition has been initiated by the government bodies and some well-known financial institutions. They have also taken the initiatives to frame policy regarding merger and acquisition necessary to adopt for Indian corporate sector.

Merger

According to the Oxford Dictionary "Merger" means "combining of two companies into one".

The term 'Merger' is not stated anywhere in sections 390 to 394 of old companies Act, 1956. The Income Tax Act, 196 has also overlooked it. The term of 'Merger' is mentioned only in accounting standard 14 given by ICAI and that is 'Amalgamation in nature of Merger'

But the new Companies Act, 2013 explains the concept of merger without specific definition. The act mentions following points about merger:

- ❖ A combination of two or more entities into one.
- ❖ The desired effect being not just the accumulation of assets and liabilities of the distinct entities but organisation of such entity into one business
- ❖ Generally, in merger, the merging entities would cease to be in existence and would merge into a single surviving entity.
- ❖ Merger or amalgamation
- ❖ Merger by absorption
- ❖ Merger by formation of a new company.

Acquisitions or Take-over

If one company acquires the controlling interest in another company, it is a case of 'Acquisition or Take-Ever.

REVIEW OF LITERATURES

MARCH 2009 MUKESH BUTANI, BMR ADVISOR, It goes on the concept of ring-fencing. it could be that at a later stage the E&P business will get hived off to a new company. In that case it is logical that you have all the refining operations under one company, 2010 , MEENAKSHI BISHT, the MBA students of Skyline College situated in Delhi, the dissertation projects of "A Critical Analysis on RIL-RPL Merger". The merger will unlock significant operational and financial synergies that exist between RIL and RPL.

(2014) December, Sunil Kumar (Assistant Professor at department of commerce in Deen Dayal Upadhyaya College, university of Delhi) has written a research paper titled, "Impact of Mergers on Corporate Performance: An Empirical Analysis of Related and Unrelated Mergers" in the journal of 'Indian Journal of Accounting' in Vol XLVI(2), of December 2014, ISSN -0972-1479 page 49-69. The said article is prepared to examine the impact of M&A on corporate performance on the basis of relatedness and on the basis of time period by selected parameters. Those parameters were sales growth, return on net worth, post-tax rate of Return on Equity assets, Total Assets Turnover Ratio, and Earning per Share. Researcher has collected the secondary data from CMIE data source and website of BSE and NSE of 60 companies. The data has been collected for total 10 years period i.e. five year before the merger and five year after the merger. Author has analysed the data by paired t-test and variation in performance is also analysed by the ANOVA technique. The data shows that the performance of unrelated merger has improved more than related merger.

(2015) A Thesis submitted by Jayaram siddalingya titled, "Effectiveness of Mergers and Acquisitions on overall performance – A case study of selected tata group companies in India" in department of post-graduation studies and research in commerce, Gulbarga University, Gulbarga. In this research study, researcher has focused his attention towards four case studies of Tata group company's merger deals - Tata finance acquired by Tata motors (2005), Usha Ispat company acquired by Tata metalinks (2006), Rawmet industries pvt. Ltd. acquired Tata steel (2007) and Coastal Gujarat power company acquired by Tata Power (2007). He has analysed the data by comparing five years' average of before the merger and after merger and has calculated the paired t-test.

(2015) January Abhimanyu Sahoo has written a research paper titled, "Post-Merger Liquidity and Solvency Position:

An Empirical Analysis of selected companies in India" at Orissa Journal of commerce with ISSN no. 0974-8482. Author has analysed the effect of merger on liquidity and leverage standards of the surviving companies after the diversified merger. He has selected 7 companies as a sample for a period ranging from 8 to 10 years during the period of 2000 to 2010. He has taken three ratios i.e. current ratio, quick ratio and debt-equity ratio and has collected the secondary data to analyse with paired t-test. By doing the said analysis, he has found that the M&A could not improve the liquidity performance and operating performance of the company.

(2016) January, 17 Heena Pahuja and Samridhi has written research paper title, "Impact of Mergers and Acquisition on India's Economy" presented for 3rd International Conference on Science, Technologies and Management, New Delhi. The authors have presented the paper on theory basis. In their paper they mentioned the merger deal between the Tata and Cores and also mentioned the merger deal between the Vodafone and Hatchison Essar company. They have presented one table which is showing the trends of mergers and acquisition from 1995-96 to 2006-2007. They have also suggested at the end that how to prevent from the failure of the merger of acquisition.

(2016) Jan-Feb., Ketan Kumra and Manvi Gupta has published research paper titled, "Comprehensive Research on the Performance of the Acquiring firms Pre and Post-Acquisition in the Pharmaceutical Industry" in volume 7, ver. II of IOSR journal of Economics and Finance, ISSN : 2321-5921, pp 10-17. This paper is published to examine the impact of two significant acquisitions in the recent past in the pharmaceutical sector considering the acquisition of Ranbaxy Laboratories Limited by Daiichi Sankyo Company, Limited and Piramal Healthcare Limited by Abbott Laboratories on the acquiring firms respectively to inspect whether the deal led to a profitable situation or not. The authors of this paper have attempted to draw a comparison between pre and post-acquisition financial performance in terms of performance ratios of the acquiring firms. The outcomes of the paper suggest that the effect on operating performance of both the acquiring firms, post-acquisition was not significant from statistical point of view.

RESEARCH METHODOLOGY

Objectives of Study

The research work emphasizes on to analysing the impact of financial performance of acquirer companies. To judge and to conclude this research problem in a best way, the following objectives are framed.

- To study the impact of merger and acquisition on financial performance of the selected financial service companies.
- To analyze upturn in earning power of the selected acquirer companies by comparing the performance of pre-merger and post-merger.
- To identify the industries which mostly adopt the way of merger and acquisition for the expansion of the business and how many of them are successful?
- An attempt to do limited research on the topic of merger and acquisition occurred in Indian industry.

Hypothesis

H0: Post-merger period hasn't improved the performance of acquiring firms. ($H_0: \mu_{Before}-\mu_{After}$) is equivalent to the statement – ($H_0: \bar{D}=0$)

And

Ha: Post-merger period has improved the performance of acquiring firms. ($H_a: \mu_B<\mu_A$) as the study is conducted to conclude that merger has been effective.

Sampling Plan

The study has been carried out on the micro-level, as it is very difficult to conduct it on the macro-level within the definite period of time and due to money constraint also. The population of the study consists of all the merger deals were made in financial service companies. i.e. 146 merger deals as per authentic data source of CMIE. (Source: CMIE – Business beacon)

Sample Size: 14 Acquirer Indian companies.

Sampling Method: Stratified sampling (on the basis of proportion)

Sample Selection: 10% Sample of population

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❖ **List of selected Samples**

Table 1.1 - Financial Services Industry

Sr. No.	Target Co.	Acquirer	
1)	Innovative Money Matters Pvt Ltd.	Avonmore Capital & Management Services Ltd.	14
2)	Ganesh Bank Of Kurundwad Ltd.	Federal Bank Ltd.	
3)	India Infoline Securities Pvt. Ltd.	India Infoline Holding Ltd.	
4)	I-yen Interactive Ltd.	Infomedia Press Ltd.	
5)	Pipavav Power Company	JPT Securities Ltd.	
6)	Keynote Finstock Ltd.	Keynote Corp. Services Ltd.	
7)	M T L Share & Stock Brokers Ltd.	Master Capital Services Ltd.	
8)	Pioneer Tradestock Pvt. Ltd.	Pioneer Investcorp Ltd.	
9)	Rain Calcining Ltd.	Rain Industries Ltd.	
10)	Luxury Exports Pvt. Ltd.	Royal India Corporation Ltd.	
11)	Sam Global Securities Ltd.	S M C Global Securities Ltd.	
12)	M B L Investments Ltd.	Sabmiller India Ltd.	
13)	Unnati Financial Services Pvt Ltd.	SE Investments Ltd.	
14)	Sugal & Damani Share & Stock Brokers Pvt. Ltd.	Sugal & Damani Share Brokers Ltd.	

DATA COLLECTION AND DATA ANALYSIS OF CASE STUDY

The data used for this study has been finally collected from CAPITALINE Plus database from the library of IIM Ahmedabad library.

The data has been collected in the form of DuPont ratios to analyse the return on investment with respect to the firm's profitability, efficiency, and leverage by following ratios:

- ❖ Tax Burden Ratio
- ❖ Interest Burden Ratio
- ❖ Operating Income Margin Ratio
- ❖ Assets Turnover ratio
- ❖ Leverage Ratio
- ❖ Return on Equity Ratio

Pre-merger and post-merger performance ratios were set for this acquisition during the period before and after five year of the acquisition average pre-merger and post-merger financial performance ratios were compared to see if there was any statistically significant change in performance due to mergers, Take difference of variables with its mean and find standard deviation out of the deducting averages.

Using " t-test : Paired two sample for means".

Significance of the Study

One of the most important elements of a research study is the significance of the study. It shows the importance of the time that is spent for the research work. The study must be useful to researchers and others to also. Below is the list of the parties to whom the study will help to increase the knowledge about the facts and findings of mergers and acquisitions:

To Acquirer Company:

Acquirer companies may know the impact of merger on earning power capacity.

The research will help the acquirer firm to know, whether they are successful in implementation of expansion strategy or not?

They can get the information about the improvement of return of 5 years' average on equity share capital compared to pre-merger return of 5 years' on equity share capital.

They should get familiar with the information about increase or decrease of all their ratios of return on earning.

To Shareholders of the acquirer company:

Shareholders have the right to know whether the company has taken the right decision or not.

The study helps the shareholders by giving the information about their benefits on investment.

To Economy:

- ❖ The study will help the regulatory authority to regulate the mergers and acquisitions deals for stakeholders' benefit like RBI and SEBI.
- ❖ The customers and the consumers also get the information about the trend of mergers and acquisitions.
- ❖ To Consultancy/Advisory firms:
- ❖ Research will help the consultancy or advisory firms that in which Industry they should pay more attention to earn more consultancy fee.
- ❖ It also provides information about more successful, less successful and unsuccessful merger deals which the consultant had advised in the past.

DATA ANALYSIS

The extended DuPont equation as per new change in terms of ROE is:

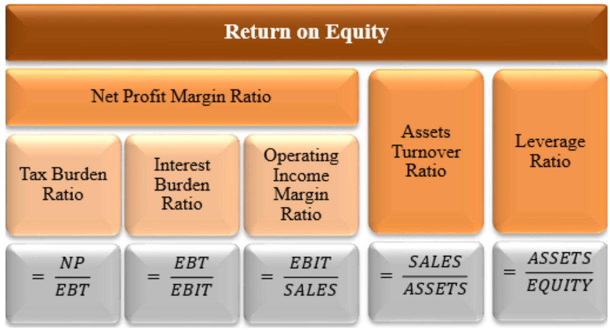

Chart 1.1

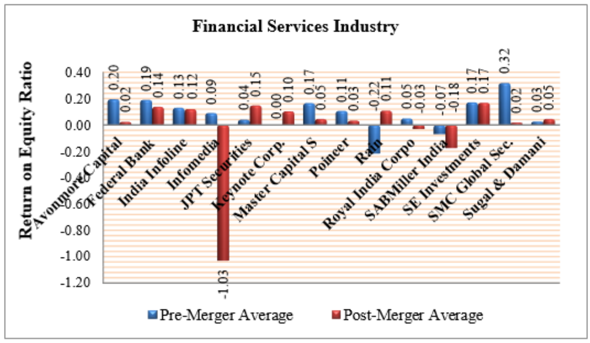

Table – 1.2 Mean of Five years' Average of all Fourteen Selected Finanacial Service Companies

Mean	Pre-Merger	Post-Merger
Tax Burden Ratio	0.99	0.84
Interest Burden ratio	0.81	0.52
EBIT Margin Ratio	0.26	-0.12
Assets Turnover Ratio	0.07	0.56
Financial Leverage ratio	2.91	2.91
Return on Equity Ratio	0.09	-0.02

Chart – 1.2

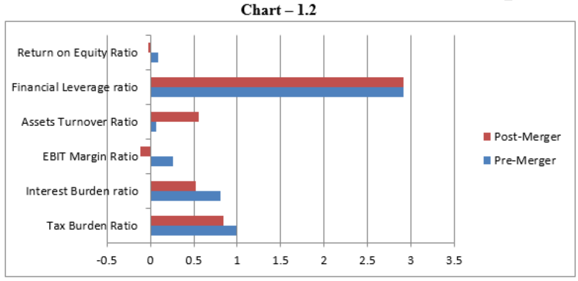

Table – 1.3 : Descriptive Statistics

Outcomes_Descriptive statistics_ all Ratios	Mean	N	Std. Deviation	Std. Error Mean
All_Ratios_Pre_Average	**0.855**	6	1.0769169	0.43964948
All_Ratios_Post_Average	**0.782**	6	1.10512292	0.45116454

Table – 1.4 : Paired Samples Test

Outcomes_Paired Differences_ Return on Equity ratio		Paired Differences				Df	t-test Sig. (1-tailed
		Mean	n	Std. Deviation	Std. Error Mean		
Pair 6	ROE_Pre_Merger_Average - ROE_Post_Merger_Average	0.07	6	0.306898	0.125291	5	0.29188049

The Calculated Value of t-test is negative 0.291 with a degree of freedom 5 and Table Value of t-distribution for the 5 degree of freedom at 5% level of significance for one tailed hypothesis is 2.015.

As it is already known that If the Calculated Value of 't' (t_c) which is always an absolute value is less than the Table Value (t_t) of 't' then Null Hypothesis (H_0) is accepted. i.e.

(|t_c | < t_t = Accept H_0).

0.291<2.015= Accept H_0

The Calculated Value of 0.291 is proved to be less than the Table Value of 2.015 which means that Null Hypothesis is accepted. Thus, the t-test result of paired differences suggests that there is no significant difference between the pre-merger performance and post-merger performance of the selected fourteen companies. Hence, the decision of merger or acquisition taken by the selected fourteen companies is proved to be insignificant for the five years period after the decision.

CONCLUSION

Though the general tendency of doing mergers and acquisitions has increased in last few years, the research study has failed to provide the evidence and disagrees with their decisions in case of selected companies. The analysis of this research has failed to proves the object of the merger to grow the company very quickly rather to opt for growing by doing normal purchasing and selling activities. The study infers that the decision regarding the mergers and acquisitions has not been able to create any positive impact on the financial performance of the selected financial service companies. The acquirer companies in financial service business have failed to satisfy their equity shareholders. However, it's wrong to say there are no such effects of merger and acquisition founds for selected companies as it might help the companies in different arena than financial performance. At the end, from the result of testing the hypothesis, it is clear that the decision of merging or acquiring the firms for improving financial performance after the period of merger or acquisition is ineffective.

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