EFFECTIVENESS OF MERGERS AND ACQUISITIONS: A STUDY OF CORPORATE ENTERPRISES FROM INDIAN AUTO-ANCILLARY, IT AND PHARMACEUTICAL SECTORS

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by

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The thesis titled, **“Effectiveness of Mergers and Acquisitions: A Study of Corporate Enterprises from Indian Auto-Ancillary, IT and, Pharmaceutical Sectors”**, being submitted by Ms.Anshu Mittal to Indian Institute of Technology Delhi for the award of the degree of Doctor of Philosophy (Ph.D.) is a record bona fide research work carried out by her. She has worked under our guidance and supervision, and has fulfilled all the requirements for the submission of this thesis, which has attained the standard required for a Ph. D degree of this institute. The results presented in this thesis have not been submitted elsewhere for the award of any degree or diploma.

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Abstract

Mergers and acquisitions (M&A), in present corporate environment, seem to have become virtually an integral part of corporate strategy. Constituting significant strategic-cum-investment decisions, the financial and strategic aspects of M&A have always been the major attraction for researchers, financial analysts, and decision-makers. Performance of M&A is inconclusive, albeit constituting one of well and largely explored aspect in literature. Most surprising part is that, the M&A activities, world-around, have shown ever increasing pace, in spite of high failure rate suggested by majority of studies. India is not an exception; in one of the recent study of Indian acquirer firms, the KPMG reports M&A failure rate of nearly seventy-five percent. The agile growth rate of M&A, notwithstanding the high failure rate, raises a question as to what inspires corporate managers for these decisions, when M&A, *prima-facie* in view of empirical studies, lead to high failure; are M&A value-creating or value-deteriorating decision?

Financial and strategic management literature reflect different view on M&A performance; strategic management literature emphasizes on intents/motives as the crucial parameter for evaluating M&A effectiveness; these studies suggest M&A to be successful strategies undertaken for the attainment of multiple corporate objectives. The non-convergence on the performance aspect of M&A and incongruence revealed from strategic and performance management literature calls for a comprehensive framework for examining M&A performance, incorporating the financial as well as strategic aspect.

In spite of wide surge witnessed in M&A investment in India, the literature seems to be deficient. The present study attempts to unify the theoretical threads of literary findings, capable of knitting together for a holistic understanding of M&A. The study attempts to integrate the strategic and financial aspects of M&A performance to get a better understanding of the core strategic intents/ motives for M&A, impact of M&A on the performance of corporate acquirer firms in India. The study pertains to three sectors, namely, auto-ancillary, IT and pharmaceutical sector.

The research has been carried out through three different phases. During first phase, conceptual frameworks of M&A intents and M&A performance have been evolved, integrating the key literary findings and opinion of experts from industry and academia. The study develops two frameworks: first, the total interpretive structural model of M&A intents; and second, the M&A performance system in terms of situation-actors-processes-performance (S-A-A-P) framework. The M&A intents system represents the hierarchical framework of M&A intents, facilitating holistic insight of the core strategic intents for M&A,

their driver-dependence relationships and interpretive cause governing the relationships. The framework has been validated in Indian context,using experts' opinion; survey findings corroborate M&A to be value-creating decisions in India driven with the intent to maximize the shareholders wealth.

The M&A performance system has been evolved as Situation-Actors-Processes-Performance (S-A-A-P) framework, with enterprise and customers factors as two broad perspectives; here, S-A-P portrays the lead parameters and last 'P' connotes the lag performance. Application of the proposed S-A-P-P framework for continuous management of the M&A performance has been illustrated using flexible strategy game-card, using evidences from Tata-Corus deal (April, 2007).

In the second phase, empirical analysis of M&A impact on financial performance of corporate acquirer firms have been conducted. For short-term impact, abnormal returns on M&A announcement have been measured using well-established event study methodology; findings are suggestive ofM&A announcements as positive news leading to significant positive abnormal returns to the shareholders of acquirer firms around announcement. However, impact is temporary and generally persists for a week, with profound impact on the announcement day or closer to it. Findings have suggested difference in the stock-return behaviour across sectors; investors' response for IT sector has been observed better in terms of magnitude of abnormality in stock-returns as well as size of conducive window showing positive abnormal returns.

Long-term financial impact of M&A has been examined using comparative analysis of pre-acquisition year performance and post-acquisition performance of consecutive three years. For the purpose, a comprehensive set of thirty-six financial ratios relating to profitability, liquidity, solvency, and growth have been used; additionally, relative efficiency scores have been measured using 'data envelopment analysis approach'. M&A did not emergedas financially viable decisions, in long-run. No significant betterment has been observed in the financial performance of the acquirer firms in terms of profitability and rates of returns; acquirer firms have shown no significant cost-synergies contributed by M&A, in terms of production, purchase of raw materials, finished goods, labour costs, administrative expenses, etc., with an exception to collusive gains in terms of reduced selling and distribution expenses and advertisement costs. From the perspective of liquidity and solvency positions, favourable impact has been observed; specifically for IT sector, desirable utilization of sizable cash resources available and unused debt capacity has been noted.Assets turnover ratio for the acquirer firms has shown a decline, for all the sectors respectively, *prima-facie,* signifying M&A failure to justify the pooled resources of acquisition. Findings have indicated difference in the magnitude of performance across sectors; profit margins of the IT and pharmaceutical sectors more or less appear to be stable *vis-a-vis* auto-ancillary sector.

The study has examined managerial views on the M&A intents and impact of M&A on the lead and lag parameters, using questionnaire survey. Based on the findings, validated integrated structural equation model (SEM) of M&A performance system has been developed.Findings are suggestive of M&A intents, enterprise processes perspective, and customers' perspectives have been identified as predictors for M&A performance. In other words, M&A performance is a function of enterprise situation, actors, processes, and customer perspective.

Additionally, six case studies have been attempted. Case findings lend support to the empirical findings as well as conceptual frameworks; all the cases analyzed indicate M&A to be a value-maximizing decision, driven to maximize the firm's value. M&A are effective strategies and help the acquirer firms in attaining their underlying intents. Case findings do not corroborate the realization of cost-synergies by acquirer firms from M&A or betterment in profit margins or rates of return. The findings of the case studies have confirmed most of the path relationships, suggested by the SEM validated framework of M&A performance system, implying the practical relevance of the framework in real life context.

In view of these findings, M&A do not seem to be profitable and successful business ventures/ propositions (in long-run), as was expected from them. M&Amore likely seem to be the strategies used by corporate firms for the attainment of manifold objectives. Cost-economies, as expected due to large scale or resource sharing, perhaps seem to be a distant possibility in present competitive environment. In this view, attaining cost-competitiveness and sustainable growth, meeting market challenges (domestic as well as international) better, acquiring brand-name, collusive synergies by merging with competitors, portfolio enrichment (by acquiring new technology, skills, expertise or scarce resources), ease to market entry, enhancing customer base, etc. seem to be more practical rationales for corporate firms in India.

M&A provide an access to pooled resources, better infrastructure, assets base, skill, expertise, market-base, and so on; these pooled resources perforce should augment/yield better performance. Declined profitability in relation to pooled resources, contrary to the expected improvement, reflects underutilization of inherent potential of M&A by the acquirer firms. This calls for an imperative need to have effective integration approach; proper assessment of pooled assets/ resources and opportunities offered by M&A, in conjunction with pre-planned integration strategy could be valuable measures in transforming M&A into successful financial ventures.

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