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AN ANALYSIS OF MOTIVES OF INDIAN ACQUIRING FIRMS

Jinomol P
Jinomol.p@saintgits.org

Dr. Roji George
roji.george@saintgits.org

Abstract

Mergers and Acquisitions (M&A) have been viewed a very important strategy of inorganic growth by firms all over the country. Large number of studies has been undertaken in order to measure the performance of the firms that involve in M&A activities. There is only limited number of studies that looks into the reasons behind M & A s by firms. This paper is an attempt to identify the motives of M & A by acquiring companies in India. The study will help us to understand the motives of acquisition which may help in better understanding the performance of companies post merger. The study reviews the offer letter submitted to SEBI by 213 Indian acquirers during the period 2009- 2010. The study finds out expansion to be the most important motive behind an acquisition, followed by growth and consolidation. The least important motive for acquisition is synergy. The sample firms are also classified based on the industry of the acquirer. Out of the total sample Investment services industry is top among undertaking M7A during the study period. The motives of acquisitions are also classified on the basis of the acquirer industry.

I. INTRODUCTION

Mergers and Acquisitions (M&A) are taking a fast turn in India as the companies have identified inorganic growth as a core strategic initiative. This major change is supported by way of favorable government policies, economic stability and corporate investment. Gone are the days when the success of a business was solely depended on its core competency. Nowadays mergers and acquisition is viewed as the process for restructuring the company.

In India, the past several years have witnessed a tremendous increase in Merger and Acquisition activities, covering up sectors like Finance, Pharmaceuticals, Telecom, FMCG, and IT & IT enabled services (KPMG (2009)).

M&A the technique of corporate restructuring for expanding the business is the most commonly used inorganic route for growth. M&A is divided into three major types- horizontal, vertical and conglomerate. Horizontal is where the companies in the same industry integrate, companies in different stages of production integrate in vertical merger and conglomerate is where in companies acquire/merge with companies that are in different industries. Horizontal integrations are undertaken to attain economies of scale, to reduce competition and reduce the investment in working capital and fixed assets where as vertical integrations are believed bring cost reduction and assure supplies and market. The major reason for companies resorting to conglomerate merger is to reduce the risk of business.

II. LITERATURE REVIEW

Academicians and research have extensively studied the merger issues world wide. Studies can be grouped as : which measures the impact of merger on performance(Pawasker (2001), Ramakrishnan(2007)Vanitha and Selvam (2007) Mantravadi & Reddy (2008), Mann & Kohli (2008), , Fraser & Zhang(2009)), that studies the reactions on capital market (Franks et al (1977), Firth (1978), Haris (1980) Dodds and Quek (1985),and Sheel and Nagpal (2000) Abhayankara(2008)). Studies are also conducted to analyse the characteristics of merging firms(Kumar & Rajib (2007) and Hannan & Pilloff (2009)).

Another area taken up for study is to identify whether market participants are able to identify post-acquisition operational synergies at the time of merger announcement-Krishnan et.al (2009)

Berkovitch & Narayanan (1993) investigated the merger motives of 330 deals in the USA. He identified three major motives for merger- Synergy, hubris and agency. The aim was to identify the primary motives of merger among the three by studying the correlation between the target and total gains. The results of the study revealed that synergy as the primary motive for takeovers.

Walker (2000) investigated the strategic objectives and stock price performance of 278 firms that merger in the USA. He identifies six primary objectives- expanding geographically, broadening product line, increasing market share, integrating vertically, diversifying with potential overlap and diversifying with no overlap. The event study result shows that the acquiring firm shareholders generally earn normal returns except for those with diversification as objective.

Objectives behind M&A are very important in analyzing the post merger performance. Hence this study is an attempt to identify the merger motives of firms which initiated mergers in India.

Objectives

The objective of the study is to

- Identify the motives behind M&A of Indian firms which initiated mergers.
- To differentiate the merger objectives on the basis of industry type.

III. METHODOLOGY

The population of the study consists of all the Indian acquiring firms from the year 2009-2010 to 2011-2012 which totals to 213 firms. These data was sourced from the databases of Securities & Exchange Board of India (SEBI), the capital market regulator of India. As per the norms, companies initiating mergers need to submit required information to SEBI which includes the objectives of merger. The researchers gathered this information from SEBI database and reviewed to identify the objectives of merger. We did not consider mergers which are initiated

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by individuals and that of foreign firms. The final sample consists of 138 firms after eliminating those deals in which individual persons are acquirers and which includes firms which are not of Indian origin.

Table 1 exhibits the description of sample based on their industry. The number of firms merged during the assessment period and their percentage is shown in the table.

Table 1: Industry based description of sample

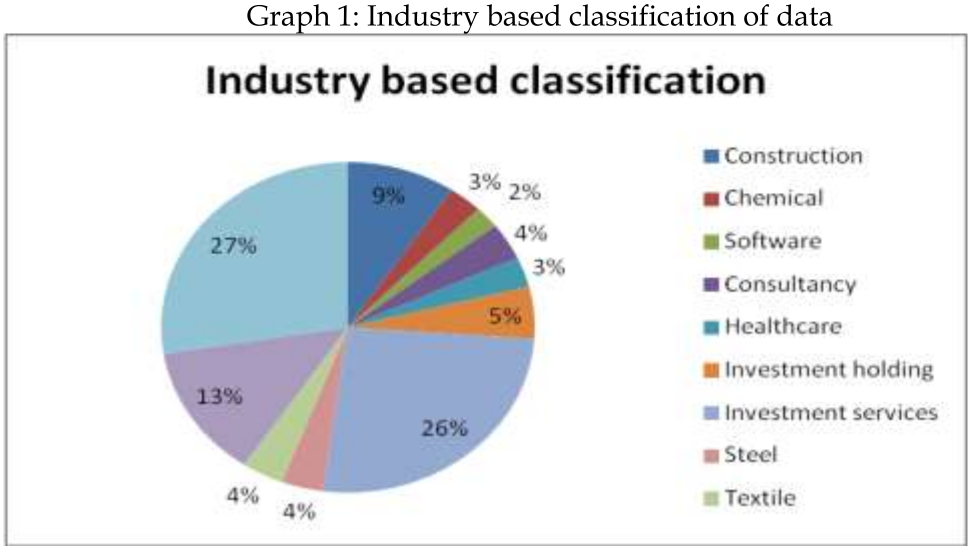
Sl. No.	Industry	No: of firms	Percentage
1	Construction	13	9.42
2	Chemical	4	2.90
3	Software	3	2.17
4	Consultancy	5	3.62
5	Healthcare	4	2.90
6	Investment holding	7	5.07
7	Investment services	36	26.09
8	Steel	5	3.62
9	Textile	5	3.62
10	Trading	18	13.04
11	Others	38	27.54

Source: Compiled by the author from SEBI Database

The sample firms are classified into ten industries. It is found that M&A is most popular in investment services industry with 36(26.09%) firms representing the total firms. Trading industry comes second with 18 firms representing this industry (13.04%). Construction industry represents 9.42% of total firms with 13 firms merging during the assessment period. The investment holding company represents 5.07% of total firms. Consultancy, steel and textile industry represents 3.62% each of the total firms. Healthcare and chemical industry represents 2.90% each and software industry represents 2.17% of total firms. The other industries include pharmaceutical, tea, apparels, automobiles, beverages, BPO, cement, power, education, FMCG, Hardware, Film, Music, mining etc. Altogether they constitute 27.54% of the total firms.

The following pie chart depicts the data on sample description based on industry.

Graph 1: Industry based classification of data



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IV. FINDINGS AND DISCUSSIONS

In the first stage of analysis, this study identifies the main objectives of merger. Table 2 illustrates the results after segregating the samples on the basis of objective. It is found that the major objective for acquisition has been identified as expansion. Around 32 percentage of acquiring firms falls under this category. This indicates that majority of the acquiring firms choose the inorganic method for expanding their business. Study found the second reason of merger is growth. Around 29 percentage firms from the sample have chosen M&A activity for the purpose of growth.

Consolidation of promoter's stake in the target firm is the third major objective identified. In Indian business world consolidation of group of companies' holdings has become very relevant in the new era. The primary objective is to increase the stake in the group and there by increasing the control over the firm. Tata Sons holding company consolidating its group is the best example always.

The other motives are to make use of the synergetic benefits or to diversify the business of the acquirer. About 11 percentage of the sample firms views M&A as a strategic investment. It is also noticed that firms take over other firms to satisfy their working capital requirements.

Table 2: Classification on the basis of Objectives

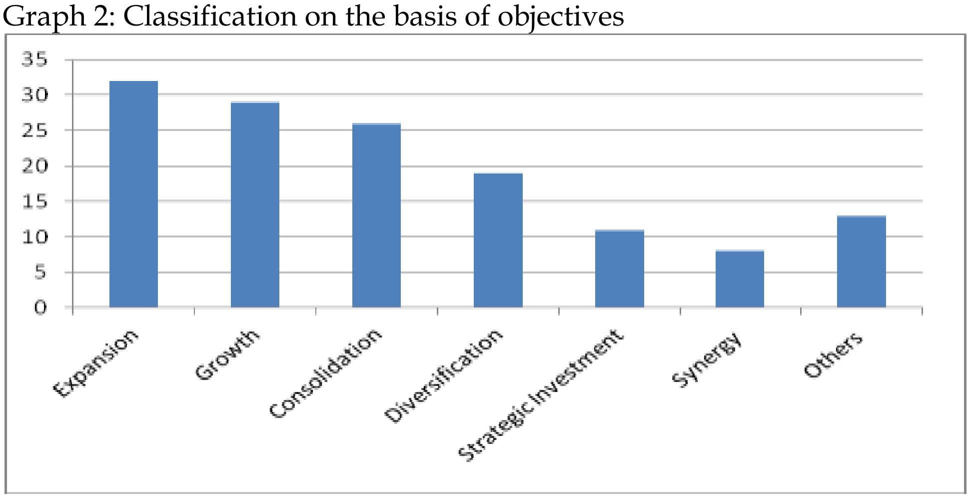
Sl. No	Objective	Number of firms	Percentage
1	Expansion	32	23.19
2	Growth	29	21.01
3	Consolidation	26	18.84
4	Diversification	19	13.77
5	Strategic Investment	11	7.97
6	Synergy	8	5.80
7	Others*	13	9.42

Source: Compiled from SEBI Database

*this includes legal requirement and working capital requirement

The following graph represents the number of firms classified on the basis of objectives of merger.

Graph 2: Classification on the basis of objectives



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In the second stage, we analyzed the objectives of merger, based on industry to test whether industry differences influences the objectives of the merger. Details are exhibited in table 3.

Table 3:Industry Classification of acquiring firms on the basis of motives

Sector	**No of firms**	**Objective**	**No:of firms**	**Percentage**
Construction	13	Growth	3	23.08
		Expansion	6	46.15
		Diversification	2	15.38
		Consolidation	2	15.38
		Synergy	0	0
		Strategic Investment	0	0
		Others	0	0
		Total	13	100
Chemical	4	Growth	1	25
		Expansion	0	0
		Diversification	0	0
		Consolidation	0	0
		Synergy	1	25
		Strategic Investment	1	25
		Others	1	25
		Total	4	100
Software	3	Growth	0	0
		Expansion	2	66.67
		Diversification	0	0
		Consolidation	0	0
		Synergy	0	0
		Strategic Investment	0	0
		Others	1	33.33
		Total	3	100
Consultancy	5	Growth	1	20
		Expansion	1	20
		Diversification	1	20
		Consolidation	0	0
		Synergy	0	0
		Strategic Investment	1	20
		Others	1	20
		Total	5	100
Health Care	4	Growth	1	25
		Expansion	1	25
		Diversification	0	0
		Consolidation	1	25
		Synergy	0	0
		Strategic Investment	0	0
		Others	1	25

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		Total	4	100
Investment Holding company	7	Growth	2	28.57
		Expansion	1	14.29
		Diversification	1	14.29
		Consolidation	0	0
		Synergy	1	14.29
		Strategic Investment	0	0
		Others	2	28.57
		Total	7	100
Investment Services	36	Growth	8	22.22
		Expansion	8	22.22
		Diversification	3	8.33
		Consolidation	11	30.56
		Synergy	0	0
		Strategic Investment	3	8.33
		Others	3	8.33
		Total	36	100
Steel	5	Growth	0	0
		Expansion	1	20
		Diversification	0	0
		Consolidation	2	40
		Synergy	1	20
		Strategic Investment	1	20
		Others	0	0
		Total		
Textile	5	Growth	1	20
		Expansion	0	0
		Diversification	1	20
		Consolidation	1	20
		Synergy	1	20
		Strategic Investment	0	0
		Others	1	20
		Total	5	100
Trading	18	Growth	4	22.22
		Expansion	7	38.89
		Diversification	1	5.56
		Consolidation	4	22.22
		Synergy	0	0
		Strategic Investment	1	5.56
		Others	1	5.56
		Total	18	100
Others	38	Growth	7	16.12
		Expansion	7	16.12
		Diversification	7	16.12
		Consolidation	8	25.84
		Synergy	5	12.90

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		Strategic Investment	4	12.90
		Others	0	0
		Total	31	100

Source: Compiled from the SEBI Database

Construction industry: It is found that 13 firms representing 9.4 % of firms belongs to construction industry. These firms include Pandora Developers and Infrastructure private ltd, Taranya project private limited, Eskay Infrastructure private limited etc. The major objective of merger in construction industry is expansion (46.15%) followed by growth (23.08%). Diversification and consolidation are the other reasons mentioned.

Chemical industry: In chemical industry, growth, strategic investment and synergy are the main objectives of the merger. But the study could find only four firms from this industry which merged during the assessment period. It represents around 2.89% of the total firms.

Software industry: There are only three firms representing this industry that have merged during the assessment period representing. The major motive for merger identified is expansion. All the firms in this industry have acquired firms that are in the related lines of business.

Consultancy industry: The merged firms in this industry represent 3.62% of the total firms. The merger motives identified are growth, expansion, diversification and strategic investment.

Healthcare industry: This industry represents 2.89% of the total firms. Growth, expansion and consolidation are the merger objectives identified in this industry. The firms include Dr Agarwal's Healthcare limited, Dunhil Healthcare Private limited etc. Acquired firms are from the same industry.

Investment holding: Growth is identified as the major objective for merger in this industry followed by expansion, diversification and synergy. There are seven investment holding companies that have merged during the assessment period.

Investment services industry: It is found that M&A is very popular in this industry. There are 36 firms representing 26.08% of the total firms. The major reason for M&A is identified to be consolidation (30.56%) followed by growth (22.22%) and expansion (22.22%). Diversification and synergy is also identified as motives for merger even though it is not that significant.

Steel industry: This industry represents 3.62% of the firms with five firms. One of the companies in this industry is Tata steel which has acquired two firms during the assessment period. Consolidation is identified as the major objective for merger in this industry (40%). Other objectives identified are expansion, synergy and strategic investment.

Textile industry:

The merger motives identified in this industry are growth, diversification, consolidation and synergy. It represents 3.62% of the firms. The firms have acquired related as well as unrelated lines of business.

Trading industry: This industry represents 13.04% of firms with 18 firms. The majority of the firms have taken up M&A with an objective to expand their business (38.89%). The other objectives identified are growth (22.22%) and consolidation (22.22%).

Other industries constitute 27% (38 firms) of total firms. The major objective identified is consolidation, growth, expansion and diversification.

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V. CONCLUSION

This study directed towards identifying the objectives of M&A after classifying them in industry sector.

- Study found that major objectives of mergers are expansion, growth, diversification and consolidation.
- From the study it is understood that the companies in the sample have used M&A for expanding their business geographically or to related lines of business and thereby increasing the value to shareholders.
- The study classified the motives of M & A on the basis of industry

VI. FUTURE RESEARCH

The main limitation of the study is that the objective of the study is limited to a single agenda of identifying the objectives of merger. Secondly, study considered only three years data for anlasying the data which is not sufficient to make right conclusions. Extension of study period is an area for future studies. Assessing performance of firms based on the predefined objectives could be another area for research.

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