

## CROSS-BORDER MERGERS & ACQUISITIONS (A PERFORMANCE REVIEW OF TATA GROUP OF COMPANIES)

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### ABSTRACT

*Since the last decade, participation of Indian companies in cross-border mergers and acquisitions are rising at a good pace. Almost all the major business houses in India experienced the so-called module of corporate restructuring. Here, Tata is leading the chart with more than 50 cross-border acquisitions. This research work is focused on the deals undertaken by this group since last decade (2000 to 2010). A sample of twelve companies has been taken to gauge the impact of this activity on the financial performance of the acquirer companies. The present study also examines the impact of this activity on the wealth of shareholders of Tata Group of companies. By comparing the pre-acquisition performance with post-acquisition numbers, insignificant decline is found in liquidity and solvency parameters considered for evaluation of financial performance. At profitability front, a significant decline is monitored in industry adjusted ROCE and RONW. The market reaction to this activity revealed an insignificant negative response during the event window period. A downward trend in Cumulative Average Abnormal Return (CAAR) during the event window period of 59 days is also witnessed.*

**Key Words :** Cross-border, Acquisitions, Financial Performance, Event Study and Shareholders' Wealth

### INTRODUCTION

Indian corporate sector is known for its global leaders in different business segments like Reliance, Infosys, Wipro, Mahindra and Mahindra and of course Tata. Approximately all the prominent business houses registered their name in the list of cross-border acquirers in their respective domain areas. During the last one decade, our business houses surprised the corporate world by having acquisition in U.S, U.K and other parts of Europe. Here, Tata is leading the chart with more than fifty cross-border acquisition deals. As this group is having its presence since 1868 in India. This group is known for its variety of product and services, good work culture, excellence in business and its values & ethics. Tata group deals in seven prominent business sectors; information technology, iron and steel,

engineering materials, power and energy, consumers products, chemicals and telecommunications. All the major companies of this group are part of the benchmark indices of prominent stock exchanges, i.e., S & P CNX Nifty 50 and S & P BSE Sensex of National and Bombay Stock Exchange of India respectively. In today's scenario, Indian companies acquiring foreign businesses are more common than the other way around and it is visible through the domestic and overseas acquisitions made by Tata group. Here, the prominent deals are acquisition of Tetley Group (U.K) by Tata Global Beverages, Daewoo Commercial Vehicles (U.K) by Tata Motors, Corus Steel (U.K) by Tata Steel, Citi Group Global Services (U.S) by Tata Consultancy Limited during the last one decade. This group will continue to take the acquisition route as one of the modes of growth for the over \$100 million conglomerate and keep to the path intensely (Rajan, 2013). This kind of showcase by Indian corporate lured the attention of many researchers to deal in the business of corporate restructuring. The so-called work can be served as basis for many companies to take a decision of M & A. As mentioned above, Tata is the largest group and experienced a large number of deals across the globe. So, it becomes important to conduct a study on a single group and to learn from the outcomes. This kind of study on a single group is not conducted so far in India and would be served as empirical evidence. The present study is dealing with the cross-border acquisitions deals conducted by this group in the countries like U.S, U.K, Russia, Australia, Indonesia, Morocco, Spain and Sri-Lanka. The study is covering the aspect of financial performance of acquirer companies affected due to this corporate action and stockholders' wealth of Tata group of companies over a short span of time.

## REVIEW OF LITERATURE

A study on cross-border mergers and acquisitions is now one of the favourite areas of interest of many researchers. The majority of studies are conducted outside India. Indian companies started aggressively with this restructuring option in the last decade at national and international level. A large amount of work is not conducted so far in India on this topic. The studies conducted at international level measured the impact of this activity on financial performance of acquirer companies and its impact on stockholders' wealth separately. The results of these studies are not able to generalize the common conclusion for all the sectors and economies studied earlier. The outcomes of the previous studies are contradictory and vary from country to country. So, the results derived from one country or industry cannot be directly applied to another country or industry. The prominent researches and their findings are summarized in the following paragraph.

Lowinski et al (2004), in their study, analyzed shareholders' perspective in case of domestic as well as cross-border acquisitions by Swiss companies. They took a sample of 114 domestic and international acquisitions announced by Swiss corporations during 1990 to 2001. They found no significant difference between the national and cross-border merger deals in terms of announcement effect. Franceour (2005) in his research studied the impact of international mergers and acquisitions (M & As) on the wealth of acquirer firms' shareholders. For this purpose, he took a sample of 847 M & A deals occurred during the

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period of 1990 to 2000 in Canada. The study found that acquirer firms engaged in cross-border M & As had realized efficiency gains and created value for their shareholders. Elango (2006) conducted his research on international acquisitions deals accomplished by U.S-based firms in the insurance sector during the period of 1997 to 2003. He studied the impact of these acquisitions on shareholders' wealth. The sample was based on 52 international acquisitions done by the U.S firms in 24 different countries. The event-study methodology was applied to examine the impact of international acquisition announcements on the acquirer firms' shareholder wealth. On the basis of the analysis, he found that acquirer firms had created statistically insignificant negative market returns during the event window period. Martynova and Rennboog (2006) studied the domestic and cross-border corporate takeovers realized by European companies. The period for the study was 1993 to 2001. The various attributes covered by the study were type of takeover deal, bid attitude, payment method, legal status of target firm and takeover strategy. They found that various attributes of takeovers had a significant impact on the wealth of shareholders. Hassan et al (2007) in their study analyzed M & A deals took place in U.S pharmaceutical industry. They selected 405 companies for the research during the period of 1981 to 2004. They separated the domestic U.S-based target companies from foreign-based targets, the tests suggested that mergers with domestic companies, i.e., US-based targets were not value destroying. Zhu and Malhotra (2008) examined the short-term stock market reaction towards the sample of Indian firms acquiring US firms for the period of 1999 to 2005. It was revealed by the study that the Indian stock market had positively reacted to the acquisition announcements. Wang and Liao (2008) examined the impact of cross-border takeovers on the wealth of shareholders. They took a sample of cross-border acquisitions of Western European firms during the period 2000 to 2007. The findings of the study revealed that cross-border acquisitions were proved as wealth-creating corporate activities. Zou and Simpson (2008) investigated the behaviour, at an industry level, of cross-border mergers and acquisitions (M & As) in the People's Republic of China for the period of 1991 to 2005. The study reported that many of the cross-border M & As over the past decades in China have been driven by broad fundamental factors, such as industry size and profitability. Moreover, technological intensity was significantly positively associated with the level of acquisition activity. It is found that deregulation, as a specific industry shock, affected acquisition activities significantly. Saboo and Gopi (2009) investigated the impact of mergers on the operating performance of acquirer firms. They took 54 cases of mergers between the years 2000-07. Their research work observed variations in the post-merger performance of acquirer firms in relation to type of firm acquired, that is, domestic or cross-border. They found a positive effect on the key financial ratios of acquirer firms at domestic level, while the same had found slightly negative for the cross-border mergers. Uddin and Boateng (2009), in their study examined the impact of cross-border M & As on the share price performance of the acquiring companies. The study applied event methodology to analyze short period share price performance. They took a sample of 373 acquisitions over a period of 1992 to 2003. The study revealed that

the U.K. acquisitions did not fetch statistically significant positive returns in the shorter period. Stieble (2011) analyzed the impact of cross-border M & As on the financial performance of investing firms in the U.K and France that went for this activity during the period 2000 to 2007. They concluded that cross-border deals enhanced the acquirer companies' domestic sales and investment after the merger and acquisition deal.

## **NEED AND SCOPE OF THE STUDY**

The present study is based on the international acquisitions undertaken by Tata group. This group is pioneer in cross-border deals and done with more than fifty acquisitions in approximately fifteen different countries. The outcome of present study will help the Indian companies to pursue this module of corporate strategy. Here, the study is considering the aspect of financial performance and shareholders' wealth of Tata group of companies; those are listed on prominent stock exchanges in India, i.e., National and Bombay Stock Exchange.

## **OBJECTIVES OF THE STUDY**

1. To analyze the impact of acquisitions on the financial performance of acquirer companies.
2. To examine the instantaneous impact of acquisitions on the wealth of shareholders of acquirer companies.

## **HYPOTHESES OF THE STUDY**

1. *Ho (1): Post-acquisition financial performance of acquirer companies is not significantly indifferent from pre-acquisition financial performance.*
2. *Ho (2): There is no significant impact of acquisitions' announcement on the wealth of acquirer companies' shareholders.*

## **RESEARCH DESIGN**

The present empirical study is validating the impact of cross-border acquisitions on the financial performance and shareholders' wealth of Tata group of companies. The sample comprises twelve cross-border acquisitions in eight different countries during the period of 2001 to 2010. Financial data related to three year prior and after this deal is taken to evaluate the financial performance. So, M & A deals after the year 2010 are not considered for. Those companies, which are listed on Indian stock exchanges, considered for sample selection.

## **DATA COLLECTION**

Secondary financial data is collected to achieve the objectives of the study. Data belongs to financial parameters of each acquirer company along with its corresponding industry averages is compiled from the prominent database CAPITALINE. To examine the impact of acquisitions on the wealth of acquirer companies' shareholders, the daily share prices

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along with values of bench mark index (S & P CNX Nifty 50) is collected from the official website of National Stock Exchange (NSE).

**RESULTS AND ANALYSIS**

Financial Performance of acquirer companies is evaluated by considering their liquidity, profitability and solvency position. The relevant data required for the study is collected from the prominent data base CAPITALINE. All the relevant financial parameters to justify the liquidity, profitability and solvency positions (Table-1) are adjusted with the corresponding industry numbers. The average value is taken for these adjusted numbers on the basis of three years prior acquisition financial performance. The same calculations are also done for post-acquisition period and compared with each other. Student t-test is applied on these tabulated values and it is evident from the results that there is no significant change in the liquidity position. Marginal decline is noticed in industry adjusted current and inventory turnover ratio, whereas a marginal positive change is witnessed in industry adjusted debtors turnover ratio. As far as solvency position is concerned, pre-acquisition and post-acquisition position is not statistically significant but marginal improvement is there in industry adjusted debt-equity and long term debt to equity ratio. But, the deterioration in profitability ratios led to decline in interest coverage ratio. Finally, profitability margin changes are not significant in case of industry adjusted profit before interest and tax and cash profit margins, but a significant decline is noticed in case of industry adjusted ROCE and RONW. The value change in case of ROCE during post-acquisition period is significant at 10% level only (t-value=1.796), whereas decline registered in case of RONW is significant at 5% level (p-value=0.048<0.05). It can be considered as a negative sign for the shareholders of the acquirer companies. Broadly, these all results lead to the acceptance of first null hypothesis, as pre-acquisition performance is quite similar as compared to post-acquisition performance.

**Table 1 : Comparative Results of Financial Parameters between Pre-and Post-acquisition Period**

Financial Parameters (Industry adjusted)	Mean Values	Mean Differentiation	Dispersion	t-Value	Significance (two-tailed)
Current ratio (b)	1				
Current ratio (a)	0.996	-0.004	0.36	-0.035	0.972
Inventory turnover ratio (b)	1.263				
Inventory turnover ratio (a)	1.15	-0.113	0.574	-0.635	0.54
Debtors turnover ratio (b)	0.987				
Debtors turnover ratio (a)	1.16	0.173	0.497	1.204	0.254
Debt-Equity ratio (b)	0.947				
Debt-Equity ratio (a)	0.838	-0.109	0.622	-0.571	0.58

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Long term debt equity ratio (b)	0.814				
Long term debt equity ratio (a)	0.803	-0.011	0.411	-0.098	0.924
Interest coverage ratio (b)	2.044				
Interest coverage ratio (a)	1.186	-0.858	2.842	-1.045	0.318
Profit before interest and tax (b)	1				
Profit before interest and tax (a)	0.996	-0.004	0.36	-0.035	0.972
Cash profit margins (b)	0.9				
Cash profit margins (a)	1.422	0.522	1.145	1.578	0.143
ROCE (b)	1.347				
ROCE (a)	0.855	-0.492	0.95	-1.796	0.100*
RONW (b)	1.505				
RONW (a)	1.051	-0.454	0.427	-2.6	0.048**

**Source:** Authors' Calculation from the data compiled from CAPITALINE database (<http://www.capitaline.com>)

\*\*Values significant at 5% level, \*Values significant at 10%\* level.

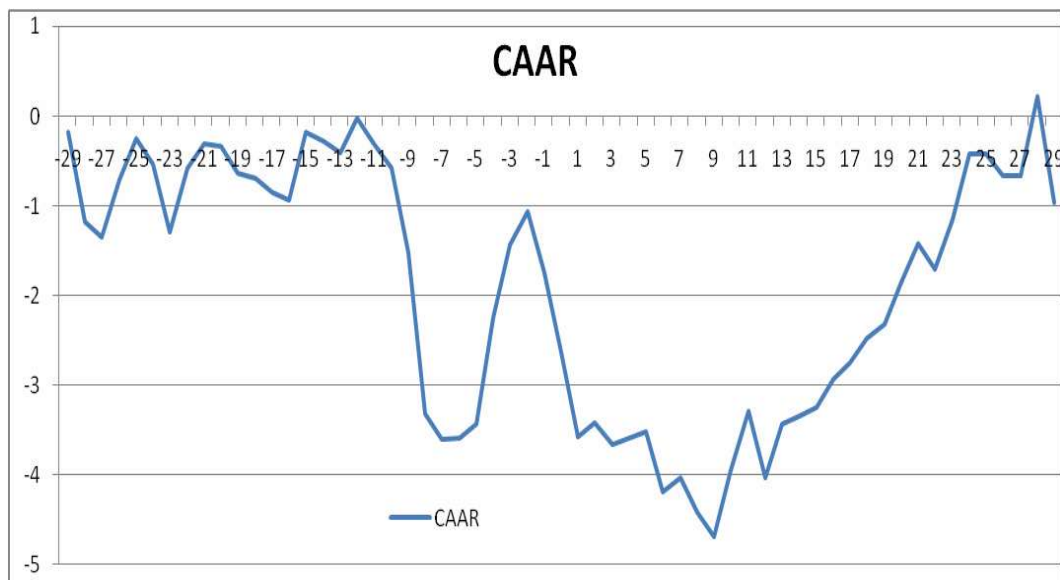
**Note:** (a) Denotes post-acquisition period. (b) Denotes pre-acquisition period.

Further, to achieve the second objective, market model of event study methodology is applied. Hence, the abnormal returns of all the sample companies are predicted on the basis of following.

$$AR_t = R_t - E(R_t)$$

Where ART is the excess return on the stock for the day 't' and 't' depicts the day relative to an event,  $R_t$  is the actual return on the stock for the day 't' and  $E(R_t)$  is the predicted rate of return on the security for day 't'. With this application, the abnormal return (AR) for each relative day (-29 to +29) for all the sample companies is calculated. The abnormal return is calculated by using capital asset pricing model for an event window of 59 days, which are 29 days prior to the announcement date and 29 days after the same. The day of announcement is designated as '0'. Beta estimation is taken for 150 days prior to the event window to estimate the expected return. The average return for all the companies averaged out for each day and t-test has been applied to check significant abnormal values (Appendix-2). It is observed from the trend that out of 59 observations (including announcement date) only three values found significant at 95% and 99% level of confidence. Out of these three values two values found prior to the acquisition announcement and one is after the same. It is evident from the (Appendix-2) the corresponding values for (-9th, -8th and 24th) days are (-2.516, -4.259 and 2.473). This shows that no major significant abnormal trend is observed during this period. The overall trend shows sluggishness for the investors. It is observed that eighteen AAR values found negative out of 29 abnormal returns related with pre-acquisition announcement period. In the second half of event window, ten AAR values found negative. The negative trend remained in the market from -29 to +9 days. The so-called trend lasted for 38 days and never allowed the CAAR to become positive.

Figure-1 Cumulative Average Abnormal Return of Acquirer Companies.



(Source: Authors' Calculations from daily stock prices and Nifty 50 values available at <http://www.nseindia.com>)

The positivity that came in to the market lasted for next 20 days only, recorded as a recovery phase and finally led the CAAR to grow up to the positive level on +28th day. The above discussion shows that overall result is not statistically significant but the trend is not in the favour of the shareholders of Tata group of companies.

### FINDINGS OF THE STUDY

The outcome of the analysis shows no significant improvement in terms of liquidity, profitability and solvency position of the acquirer companies, though marginal decline is noticed in all the three relative aspects. As far as profitability position is concerned a significant decline is registered in case of ROCE and RONW. Secondly, the market reaction to this activity is very sluggish and put the market in negative zone, though this is not statistically significant.

### RECOMMENDATIONS

1. The reasons behind the marginal declines in financial parameters after the acquisitions must be indentified by the Tata Group of companies and properly addressed for its next course of action.
2. The financial aspects of target Company must be studied properly by the acquirer company to make this activity more fruitful.
3. This corporate restructuring module should be based upon the objective of maximizing shareholders' wealth.

## LIMITATIONS AND SCOPE FOR FURTHER RESEARCH

1. The given study is only considering those companies of Tata Group, which are incorporated in India and listed on Indian stock exchanges.
2. Impact on shareholders' wealth is studied for a shorter period. This can be extended for the long-term also.

## CONCLUSION

On the basis of our research it is found that the financial performance of acquirer companies registered a marginal downfall in liquidity, solvency and profitability position. Here, acquirer companies have witnessed a significant decline in return on capital employed and return on net-worth only. At market front, very few values found significant. Apart from the same, insignificant negative abnormal returns are observed during the event window, which have led to the decline in cumulative average abnormal return. The overall results at both front does not seem in favour of Tata group companies along with its shareholders.

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**Appendix-1 List of Cross-border Mergers and Acquisitions by Tata Group of Companies**

S. No.	Acquirer company (Tata group)	Acquired Company	Stake Acquired	Country	Year of Merger/ Acquisition
1	Tata Global Beverages Ltd.	Tetley Group	100%	U.K	Feb-00
2	Tata Motors Ltd.	Daewoo Commercial Vehicle Company	100%	U.K	Mar-04
3	Tata Chemicals Ltd.	Indo Maroc Phosphorus SA (IMACID)	50%	Morocco	Mar-05
4	Indian Hotels Ltd.	Starwood Group (W Hotel)	100%	Australia	Dec-05
5	Tata Steel Ltd.	Corus Ltd	100%	U.K	Jan-07
6	Tata Power Ltd	P.T Kaltim Prima Coal and P.T Arutmin	30%	Indonesia	Jun-07
7	Tata Chemicals Ltd.	General Chemicals Industrial Products (Now Tata Chemicals North America)	100%	U.S	Jan-08
8	Tata Consultancy Ltd.	Citi Group Global Services	100%	U.S	Dec-08
9	Tata Global Beverages Ltd.	Grand Ltd.	33.20%	Russia	Mar-09
10	TRF Ltd.	Dutch Lanka Trailer Manufacturers	51%	Sri Lanka	Jul-09
11	Tata Motors Ltd.	Haspano Carrocera SA	79%	Spain	Oct-09
12	Tata Communication Ltd.	B.T Group's (B.T) Mosaic Business	100%	U.K	Jan-10

Source: [http://www.tata.in/htm/Group\\_MnA\\_CompanyWise.htm?sectid=Mergers-and-acquisitions](http://www.tata.in/htm/Group_MnA_CompanyWise.htm?sectid=Mergers-and-acquisitions)

**Appendix-2 Table of Average Abnormal Returns during Event Window.**

Day (prior Merger)	Average Abnormal Return	Standard Error (Mean)	t-Value	Day (Post Merger)	Average Abnormal Return (AAR)	Standard Error (Mean)	t-Value
-29	-0.0017	0.0141	-0.4097	1	-0.0094	0.03	-1.0839
-28	-0.01	0.0193	-1.7976	2	0.0016	0.0302	0.1797
-27	-0.0018	0.0284	-0.2151	3	-0.0024	0.0188	-0.4499
-26	0.0064	0.026	0.8518	4	0.0008	0.0284	0.0919
-25	0.0046	0.0162	0.9859	5	0.0007	0.0333	0.0752
-24	-0.0028	0.0134	-0.7158	6	-0.0068	0.0178	-1.3269
-23	-0.0076	0.0149	-1.7623	7	0.0016	0.0445	0.1256
-22	0.0071	0.022	1.124	8	-0.0038	0.0527	-0.2517

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-21	0.0026	0.0217	0.4161	9	-0.0027	0.0246	-0.3843
-20	-0.0002	0.0188	-0.0452	10	0.0075	0.0217	1.1912
-19	-0.003	0.0183	-0.5639	11	0.0066	0.0187	1.2136
-18	-0.0006	0.0316	-0.07	12	-0.0074	0.0183	-1.4065
-17	-0.0016	0.0435	-0.1253	13	0.0059	0.0166	1.243
-16	-0.0009	0.0229	-0.1301	14	0.0009	0.0098	0.3124
-15	0.0076	0.0189	1.401	15	0.001	0.033	0.1065
-14	-0.0009	0.0183	-0.1788	16	0.0031	0.0171	0.6367
-13	-0.0014	0.0212	-0.2241	17	0.0018	0.0458	0.1374
-12	0.0039	0.0157	0.8585	18	0.0028	0.0174	0.5493
-11	-0.0028	0.0149	-0.6555	19	0.0015	0.018	0.2901
-10	-0.0028	0.0286	-0.3354	20	0.0048	0.0168	0.9928
-9	-0.0094	0.0129	-2.5169**	21	0.0042	0.0173	0.8519
-8	-0.0181	0.0147	-4.2595**	22	-0.0029	0.0128	-0.7943
-7	-0.0028	0.0267	-0.3631	23	0.0056	0.022	0.8786
-6	0.0001	0.0397	0.0084	24	0.0074	0.0103	2.4738**
-5	0.0016	0.0382	0.1439	25	0.0001	0.0168	-0.0177
-4	0.0118	0.0219	1.8748	26	-0.0024	0.0198	-0.4209
-3	0.0082	0.0187	1.5129	27	0	0.0233	0.0065
-2	0.0038	0.0182	0.7181	28	0.0088	0.0183	1.673
-1	-0.0069	0.0274	-0.8738	29	-0.0118	0.0356	-1.1492
0	-0.0088	0.0262	-1.1635				

**Source:** <http://www.nseindia.com/products/content/equities/equities/equities.htm>

**Note:** Values significant at 95% level of confidence \* Values significant at 99% level of confidence\*\*