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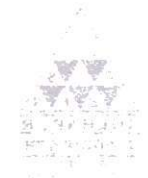
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## Editorial Note

In India with the change of guard at the centre there is lot of hope and expectations from the new regime. New policies and areas of focus are sending positive signals to the business communities in India and abroad. Discussions are already taking place on various platforms regarding environment protection, improving the business climate, reviving the lagging sectors and others. Accordingly in the present issue we have chosen the research work done on these related themes. The first article takes up the issue of environment. The author summarizes the issues and concerns in this aspect and introduces the reader to the latest terms being introduced world over in this important field. The concept of mergers and acquisitions is examined in the second research study. Based on the primary and secondary level data the authors attempt to throw more light on the trend of mergers and acquisitions taking place in the business world. With the new governments in the different states of India there is unwarranted haste to appease the farmers by way of debt waivers and debt relief. The author in the third article of this issue examines the usefulness of such schemes in the state of Andhra Pradesh. It gives useful insights into the reach and the utility of such schemes. It is concluded that instead of straining the exchequer by floating populist schemes it will be wise to design long-term asset generating schemes for the poor farmers. This will not only reduce the suicide rates being observed in different states but also help the farmer families to rise in their economic status.

In all the present issue covers the latest topics being discussed in the academic and policy making field. The rigor of these research articles and the new observations will definitely benefit the researchers and professionals in these fields.

**Dr. T. V. G. Sarma**  
Editor

# Motives for Corporate Mergers in India

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**Abstract :** Rising trend in mergers across the globe raises an important question as to why do firms merge. Several explanations and hypotheses are extended in justification for corporate mergers. Mergers and acquisitions (M&As) represent a form external adjustments carried out by the firms to adjust to the evolving environment on account of industrial deregulation and liberalization and bring about rapid changes in the size and structure of companies and the industry they belong. They may be guided by the desire to improve the value of combined entity through the generation of synergies or may be carried out to deploy excess cash flows available to resolve agency problems. Some regard mergers are a manifestation of agency problem. The present study identifies that Indian firms are generally guided by the desire to realise synergistic gains and to strengthen the competitive position of acquiring firms' vis-à-vis the suppliers and customers. Such motives are ubiquitous even among vertical and horizontal mergers. Mergers to mimic the competing firms, to be the first among the competitors and to fall in line with the international merger trends are rated very low by the managers of firms involved in mergers in India.

**Key Words :** Mergers, Acquisitions, Motives, Synergy, Managerialism.

## 1.0 Introduction:

Mergers and acquisitions (M&As) are one of the forms of corporate restructuring. Though mergers and acquisitions terms are used synonymously, generally merger term is preferred if two or more firms are combined to form another firm while acquisition is preferred if acquiring firm absorbs target without forming a new firm. Despite technical niceties, M&A world has always remained an enigma for researchers. There are years of high merger activity and years of low merger activity, called as merger waves. Further, merger failures are also high. Conservative estimation indicates that nearly 60% mergers end in failure. Risk of failure is more in big mergers than in small mergers. Despite these risks, firms do merge and mergers occur in waves.

The global corporate sector has evidenced six waves of M&As in last 100 years (Gaughan, 2007). Those are early 1897-1904

(horizontal mergers), 1916-1929 (vertical mergers), 1965-1969 (conglomerate mergers), 1984-1989 (strategic alliances), and 1992 - 1997 (mega deals) and 2003-2007 (strategic and cross border deals). Since 2011, the M&As have increased rapidly in terms of number of deals and value of deals indicating the emergence of seventh merger wave.

Firms merge for varied reasons. The academia classifies them into economic or rational motives and dubious motives. Sometimes merger motives could be personal. Several explanations have been extended in support of merger motives. In reality, mergers are justified only if they increase the value of combined firms. The sources of value increases may be due to synergy gains, elimination of competition and consequent wasteful utilization of resources, elimination of duplicating activities, tax savings, improved bargaining power vis-à-vis suppliers and

customers, increased power, etc.

Mergers can be justified on all these counts. However, mergers reducing risk through diversification is viewed as dubious in view of the fact that shareholders can also diversify and their diversification is easier and less expensive. There are arguments in support of diversification as a rational motive for mergers. Diversification becomes necessary and value adding in case of owner-managed firms; to retain reputation capital, to carry forward brand and other intangibles developed, for unlisted firms, listed but not regularly traded, etc. Mergers are also justified because they reduce excess funds in the hands of managers and force him to tap capital market sources of funds. A merger or takeover can help in resolving agency problem by removing inefficient or indisciplined managers by the acquiring firm.

A merger may be motivated by personal reasons of managers. The academic puts this in the form 'managerialism' or 'managerial entrenchment' argument. A manager may use merger to grow himself and his coterie. Merger increases manager's power and makes him indispensable. Further, merger increases size and size of the firm in turn increases manager's compensation.

Analysis on the lines of motives would help us to understand the basic reason for which firms merge. Do firms merge for synergy purpose or diversification purpose or for personal reasons? Generally, society gains when merger motives are economic and loses when mergers are driven by personal goals of executives. Mergers which lead to reduction in number of competitors are generally discouraged the world over and there are anti-trust regulations against mergers restricting the competition. Merger gains depend on merger

motives. The market performance and financial performance depend on the reason for the merger. A merger with economic motive performs better than others. Similarly, a merger with personal motive fares poorly from shareholders' perspective. There exist a vast extant literature on the analysis of both market and financial performance. Why do Indian firms merge? What explains for merger motives in India? Are they strategic or personal in nature? Do merger motives are uniform across countries? The present study aims to answer some of these questions.

## 2.0 Review of Literature

Merger and acquisition (M&As) have been extensively researched both in the West and the East. The areas covered so far include wealth effects of mergers for bidders and targets around announcement date (Jensen, 1983), estimation of merger synergies (Mueller et al. 2003), impact of methods of payment (Shleifer and Vishny, 2003), long-term performance (Agrawal and Jaffe, 2001), the managerial hubris (Roll, 1986), merger prescriptions (Trautwein, 1990), industry clustering (Mitchell and Mulherin, 1996) etc. Some others have concentrated on post-merger performance Agrawal and Jaffe (2001), merger waves (Harford, 2005).

In India mergers and acquisitions have gained importance in the recent period, particularly after 1991 (Beena, 2000). Beena (2004) analyses merger waves in India. Agrawal and Bhattacharjea (2004) finds that mergers in India are occurring in response to regulatory shocks; Kumar (2000) analyse the pattern and implications of M&As by MNEs; Guruswamy and Radhakrishnan (2010) analyse the pre and post acquisition performance; Hyderabad (2013) measures long term post merger share price performance of acquiring companies in India and Mantravadi and Reddy

(2009) analyses the impact of type of merger on operating performance.

There are several studies undertaken by the researchers to map the merger motives. Merger motives can be studied by observing market reaction to merger announcement, by computing long-term post-merger performance or by eliciting the opinion of CEOs and/or CFOs involved in the merger process. According to short-term market reaction method, a positive return could be taken to mean as 'merger for synergy' while a negative return could mean as 'managerialism' motive. Similarly, positive and negative long-run returns to the shareholders could be inferred.

Arnold and Parker (2009) employ the market performance approach to identify motives and employ 63 merger cases of UK between 1989 and 2003. A positive gain to merging firms is a 'synergy motive' and a gain to target only is taken to mean 'managerialism motive' as bidder pays a premium to acquire the target. On the other hand, 'hubris motive' is assumed if initial gains to targets are positive but overall gains are zero, due to random nature of the valuation errors being made. The study concludes that synergy and hubris hypotheses dominate as motivations for mergers.

Berkovitch and Narayana (1993) adopt 'market returns' as a method to understand merger motives for 330 tender offers of the period 1963-1988. The study presumes three motives for mergers – synergy, agency and hubris and looks at the correlation between target and total gains. A positive correlation is taken as an indicator of synergy motive, negative motive as agency motive and zero correlation to mean hubris motive. The empirical evidence shows that synergy is the primary motive in takeovers with positive total gains even though the evidence is consistent

with the simultaneous existence of hubris. The study also finds that agency is the primary motive in takeovers with negative gains.

Seth et al (2000) employ a method similar to Berkovitch and Narayana (1993) for 100 foreign acquisitions of US firms for 10-year period 1981-1990. The study shows that synergy explanation as the predominant explanation. However, hubris hypothesis co-exists with the synergy hypothesis. The study estimates a total gain of 7.6% of the pre-acquisition value of the combined firm or \$249 million positive total gains in 74% of the acquisitions. The targets realize majority of the gains while acquirers realize neither gain nor lose on average. Rhoades (1998) investigate the motives through nine case studies of bank mergers in the US and finds that four out of the nine cases show efficiency gains compared to their peers. The study concludes that cost cutting was the motive behind the bank mergers.

Why do Indian firms merge? Motives cannot vary across the globe. Motives would remain the same, be it Indian mergers or US mergers. Presently mergers are driven by strategic motives. Hence, it can be surmised that Indian mergers too are driven by strategic motives. Using questionnaire method, Rani et al (2012) survey 152 CFOs, Chairmen, Company Secretaries, etc., of firms involved in M&A activities in India during 2003-2008 and identify merger motives for 568 acquirer companies involving 893 target companies. The study finds 'taking advantage of synergies' as a primary motive of merger and 'business consolidation' as a second-most important motive. Restructuring organization, organic growth, acquiring BIFR referred sick company, reduce taxes, diversification, etc., appear to be the other motives for Indian mergers.

Banga and Gupta (2012) survey 65 mutual fund managers in India through a questionnaire to examine the motives behind the mergers and takeovers of mutual fund scheme. The study finds expansion of marketing and management capabilities, expansion of asset size and benefits of diversification as three most important motives behind mergers and takeovers of mutual fund schemes in India after performing factor analysis and multiple regression analysis.

### 3.0 Need for the study:

Merger motives can vary across period, merger waves, countries, companies, type of merger, characteristics of firms involved in mergers, ownership pattern in the firm, etc. Agarwal and Sensarma (2007) argue that significant differences in motives can exist between the countries, across the industry and over the period also. Motives determine the both market and financial performance. A merger with strategic motive can generate both private and social gains. Such mergers bring about synergy gains and eliminate unnecessary costs. On other hands, managers which involve agency and hubris problems bring gains to managers rather than the shareholders.

Merger failure percentage is high and is increasing. Mergers fail for many reasons and one of the important reasons is lack of economic justification. A failed merger brings destruction to all and is a waste. It could create havoc among corporate sector. Therefore, managers can ensure merger success provided the mergers are done for economic reason.

Do Indian firms merge for economic reasons? Do these mergers are uniform across all firms or vary? Do Indian firms merge for reasons similar to Western firms? The present study aims to analyze on these lines. An analysis on these lines adds to the

understanding of merger phenomenon.

### 4.0 Objectives of the study:

The study aims to achieve the following objectives:

- To identify corporate merger motives in India
- To understand relationship between types of mergers and their motives
- To understand merger motives across industries.
- To understand relationship between method of financing and merger motives.

### 5.0 Research Methodology

The study covers corporate mergers in India during the period 1996 to 2010. The study included M&As of all the industries and uses both the primary data as well as on the secondary data. The primary data is collected from the CEOs and CFOs of the companies involved in mergers through the questionnaire method. The PROWESS database of CMIE, Mumbai is used to prepare the list of the companies involved in mergers. The same database was referred by Beena (2000) and Agrawal and Bhattacharjea (2006). There were in total 1874 mergers announced during the period 1996- 2008. In order to increase the accuracy and reliability, 587 companies listed on the BSE only were included in the sample based on the address book published by the BSE.

The questionnaire was designed after review of literature and holding discussions with many academicians and professionals in the field. In order to ensure quality of the questionnaire it was sent to the experts and their suggestions were incorporated in the revised version.

**Table -1 Rate of response**

Sl. No.	Questionnaires Sent	No of questionnaires sent	No of responses received
1	Original	587	20
2	First reminder	510	10
3	Second reminder	425	18
Total			48

Source: Compiled from primary data

Out of 587 questionnaires mailed, only 20 responses were received and the second reminder fetched only 10 responses. The third reminder was sent to increase the response rate and finally 18 responses were received. That

makes the total sample size of 48. As evidenced by Rani et al. (2012) the survey response rate in the subject of finance is poor and not encouraging.

**Table -2 State wise responses**

Sl. No.	Domicile State of Acquiring Firm	No of responses	%
1	Maharashtra	16	33.33
2	Karnataka	11	22.92
3	Delhi	2	4.16
4	Gujarat	4	8.33
5	West Bengal	3	6.25
6	Punjab	1	2.08
7	Haryana	1	2.08
8	Tamilnadu	4	8.33
9	Goa	3	6.25
10	Uttar Pradesh	1	2.08
11	Andhra Pradesh	2	4.16
	TOTAL	48	100.00

Source: Compiled from primary data

The study received 48 responses from 11 States of India. The State of Maharashtra, the home state of City of Mumbai, contributed a larger number of respondents followed by the State of Karnataka with 11 responding companies.

For the purpose of analysis, all the respondent companies were broadly classified into manufacturing and service sector. Table-3 shows classification of these responding companies:

**Table -3 Sector wise response rate**

Sl. No	Sector	No of responses	%
1	Manufacturing	27	56.25
2	Service	21	43.75
	Total	48	100.00

Source: Compiled from primary data

Manufacturing sector response rate was 56.25% and the service sector constitutes 43.75%.



Table-4 shows industry wise response rate

**Table – 4 Industry-wise Response Rate**

Sl. No.	Name of the Industry	No.	%	Sl. No.	Name of the Industry	No.	%
1	IT & Software	12	25.00	7	Plastic	2	4.16
2	Automobiles	4	8.33	8	Textile	2	4.16
3	Chemicals	3	6.25	9	Construction	2	4.16
4	Pharmaceuticals	3	6.25	10	Financial Services	2	4.16
5	Trading	2	4.16	11	Others	13	29.17
6	Banking	2	4.16		<b>Total</b>	<b>48</b>	<b>100.00</b>

Source: Compiled from primary data

Information technology and software sector account for 25% of the total sample followed by manufacturing sector. The sample includes acquiring firms from chemicals, automobiles, pharmaceuticals, plastic, textile sectors, etc. The other sector includes firms from electric, lubricants, consultancy, mining, transportation, braveries, steel, and electronic industries provided their responses one each.

## 6.0 Analysis of Data

The following pages present the analysis of data collected through questionnaires circulated among CFOs of acquiring firms. The analysis covers aspects motives for mergers, type of merger and merger motives, diversification motive, relation between merger motives and methods of financing, impact of global mergers on merger motives in India, etc.

### 6.1 Is merger a strategic motive?

The corporate firms of modern era use many strategies for their survival and growth. Gaughan (2007) opines that growth of a firm is of two types - internal growth and external growth. The internal growth is slow and uncertain but the external growth can be achieved through M&As. Firms involving in

mergers use various external growth strategy. Through merger, a firm achieves the competitive advantage or overcomes the various shortcomings or may have a first mover advantage or may try to outwit its competitors. The survey reveals nearly 92% of respondents agreeing that merger is basically a strategic move on the part of acquiring firms. This definitely augurs well for the firm concerned and can be expected to generate wealth. A merger which benefits only the top executives destroys wealth. Lubatkin (1983) showed evidences on three sources of strategic relatedness between the acquiring firms and the target firms. Those are technical economies, pecuniary economies and diversification economies. Brouthers et al (1998) also finds that in his work that mergers are done to accomplish strategic motives.

### 6.2 Specific Motives for Mergers in India

The study makes a detailed analysis of specific motives guiding merger decisions by executives in firms. Table 5 tabulates specific merger-wise motives in India.

**Table 5: Specific Reasons for mergers in India***(Figures in the brackets indicate percentages to the total respondents)*

Sl. No	Specific Motive	Strongly Agree (4)	Agree (3)	Disagree (2)	Strongly Disagree (1)	-
1	To acquire competencies not possessed internally	16 (33.33)	25 (52.08)	2 (4.17)	4 (8.34)	1 (2.08)
2	To reduce competitive pressure in the market	12 (25)	18 (37.50)	12 (25)	6 (12.50)	--
3	To use surplus cash available in the firm	6 (12.5)	12 (25)	23 (47.92)	6 (12.5)	1 (2.08)
4.	To take advantage of favourable tax climate	8 (16.67)	15 (31.25)	9 (18.75)	11 (22.92)	5 (10.42)
5	To achieve personal ambition	7 (14.58)	11 (22.92)	5 (10.42)	24 (50.00)	1 (2.08)
6	To improve the growth rate of the firm	20 (41.67)	24 (50.00)	2 (4.17)	2 (4.17)	--
7	To extend the product line and product mix of the firm	18 (37.5)	26 (54.17)	4 (8.33)	--	--
8	To enhance product capabilities	17 (37.5)	29 (60.42)	2 (4.17)	--	--
9	To obtain synergistic gains involved in mergers	20 (41.67)	28 (58.33)	--	--	--
10	To reduce risk involved in the existing business	17 (37.5)	26 (54.17)	3 (6.25)	2 (4.17)	--
11	To retain talented pool of employees	10 (20.83)	14 (29.17)	9 (18.75)	9 (18.65)	6 (12.5)
12	Be the first among the competitors	2 (4.17)	8 (16.67)	23 (47.92)	11 (22.92)	4 (8.33)
13	Mimic merger decisions of competitive firms	2 (4.17)	6 (12.5)	8 (16.67)	25 (52.08)	7 (14.58)
14	To all in line with international mergers	4 (8.33)	6 (12.5)	14 (29.17)	14 (37.5)	6 (12.5)

Source: Compiled from questionnaires.

The study considers 14 specific motives for mergers in India. Out of which, respondents agree or strongly agree for eight motives as motives for mergers in India and for remaining motives they either disagree or strongly disagree. Obtaining synergistic gains from mergers has been the primary motive for merger with 100% of sample respondents either strongly agree or agree to the motive followed by reducing risk through diversification. The other plausible motives are to acquire competencies not available, improve the growth rate, extending product line and mix, etc.

Mimicking the merger decisions of competitors, merge just to fall in line with international merger trends, etc., have been rejected nearly by 80% of respondents as motives. The other motives not accepted by managers of Indian companies are 'to be the first among the competitors, use surplus cash flows, to take favourable tax advantage and to achieve personal goals.

Studies undertaken in US and other European countries evidence some similar facts. Walter and Barney (1990) argued that there is a relative importance of merger motives across different types of mergers. Bradley et al (1988) find that a successful merger offer increases combined value of the merged entity by 7.4%. Rhoades (1998) argued that in bank mergers efficiency gains occur by cost cutting.

Table-6 shows the respondent's opinion about each statement developed to understand various merger motives. The five point Likert scale is used to measure the opinions of the respondents. The scores assigned were strongly agree- 4, agree-3, disagree-2, strongly disagree-1 and can't say-0. A weighted index score was calculated by multiplying each response with the relevant score and total score is divided by total score (10) to get the weighted score. This helps to identify the prime motives behind the mergers.

**Table - 6 Weighted Score of Merger Motives**

(Weighted score = 4\*strongly agreed+3\*agreed+2\* disagreed  
+1\*strongly disagreed+0 \*can't say/10)

Sl. No.	Motives for mergers	Weighted Score	Rank
1	To acquire competencies not possessed internally	14.7	6
2	To reduce competitive pressure in the market	13.2	6
3	To use surplus cash available in the firm	11.2	7
4	To take advantage of favourable tax climate	10.6	9
5	To achieve personal ambition	9.5	10
6	To improve the growth rate of the firm	15.8	3
7	To extend the product line and product mix of the firm	15.8	3
8	To enhance product capabilities	15.9	2
9	To obtain synergistic gains involved in mergers	16.4	1
10	To reduce risk involved in the existing business	15.4	4
11	To retain talented pool of employees	10.9	8
12	Be the among the competitors	7.7	11
13	Mimic merger decisions of competitive firms	6.7	13
14	To fall in line with international mergers	7.0	12
	Mean	12.2	
	Standard Deviation	3.56	
	Variance	12.67	

Table 6 reports the weighted scores and ranking of the respondent's opinions for the purpose of identification of merger motives. The highest score motive is ranked 1 and the least score motive is ranked 14. The analysis reveal that, synergy, enhancement of production capabilities, extension of product line and product mix and to improve the growth rate of the firm are the top three motives for mergers in India. Rani et al (2012) evidence similarly and find that obtaining operating synergy as the prime motive of mergers in India.

### 6.3 Is Diversification a strong motive for mergers?

The desire to diversify though it is said in merger literature that diversification is dubious motives. Firms diversify to smoothen out fluctuations in the earnings. Two firms with divergent correlation coefficient can reduce the

risk factor through diversification. However, individual shareholders can also diversify and such personal diversification is considered to be more economical and faster. Despite this point, conglomerate mergers are encouraged for diverse purposes. Lubatkin (1983) identifies three potential sources of strategic relatedness among acquiring firms and target firms, diversification is one of the strategic relatedness. The third merger wave of period 1960 to 1973 occurred mainly on account of diversification motive (Gaughan, 2007). Many US firms undertook merger during this period for the purpose of diversification.

The present study surveyed the opinions of CEOs and CFOs regarding the diversification motive for Indian mergers. The survey reveals some sort of confusion in the minds of Indian managers. An equal number of executives opine in both the ways, that mergers

in India have diversification motive and does not have diversification motive. Some companies diversify their business through mergers to minimize or to avoid the risks in the existing business.

#### 6.4 Types of mergers and merger motives

Mergers are of different types such as vertical, horizontal and conglomerates. Merger motives vary across different mergers. Vertical mergers aim to streamline the operational activities and realise scale economies. Though horizontal mergers, too, aim at scale economies, they could have the objective of limiting the number of competitors or increasing market share. On the other hand, diversification merger, besides risk reduction, may have personal objective of managers or may have an objective of putting the best use of excess cash flow. Baker et al (1988) hold the view that synergy is the one of the motives behind mergers, some mergers are due to financial synergies, some are due to operational

synergies and some others are due to managerial synergies.

#### 6.5 Types of mergers and their effects

Motives could vary across different types of mergers. All mergers need not always be guided by the same objective. Though operational efficiency could be the motive for vertical and horizontal mergers but the source of operational efficiency could be different. Vertical mergers help a firm to streamline its downstream and upstream lines of activity by going for backward and forward integration. On other hand, a horizontal merger, though limits competition, enables a firm to enjoy scale economies and market power. The conglomerate mergers may be carried out to deploy surplus cash or to reduce risk or sometimes to meet the personal motives of managers.

Table-7 presents the tabulated data relating to types of mergers & merger motives.

**Table: 7: Merger Types and Merger Motives**

Sl. No.	Motives	Strongly Agree (4)	Agree (3)	Disagree (2)	Strongly Disagree (1)	Can't Say (0)
1	Vertical mergers improve overall performance of merged firm	9 (18.75)	33 (68.75)	--	--	6 (12.5)
2	Vertical mergers strengthen a firm's bargaining position vis-à-vis its suppliers and customers	23 (47.92)	23 (47.92)	2 (4.16)	--	--
3	Horizontal mergers limit the competition	26 (54.17)	15 (31.25)	--	--	7 (14.58)
4	Horizontal mergers produce consolidation effect on the industry	10 (20.83)	28 (58.33)	3 (6.25)	--	7 (14.58)
5	Conglomerates are used to diversify risk	10 (20.83)	16 (33.33)	2 (4.16)	2 (4.16)	18 (37.5)
6	Managers are poorer than shareholders	20 (41.67)	3 (6.25)	5 (10.42)	3 (6.25)	17 (35.42)
7	Horizontal and vertical mergers are more successful than conglomerates	10 (20.83)	15 (31.25)	7 (14.58)	--	16 (33.33)
8	A conglomerate works like a miniature capital market, reduces uncertainty and transaction cost	4 (8.32)	16 (33.33)	12 (25)	2 (4.16)	14 (29.17)
9	Conglomerate mergers are motivated by desire to build promotional opportunities for insiders	7 (14.58)	12 (25)	10 (20.83)	3 (6.25)	16 (33.33)
10	Conglomerates arise on account of industry clustering	6 (12.50)	22 (45.83)	7 (14.58)	2 (4.16)	11 (22.92)

Source: Compiled from Primary Data

The study considers ten motives for analysis of the linkages between merger types and merger motives. 87.5% and 95.8% of respondents either strongly agree or agree that vertical mergers are accomplished to achieve improvement in overall performance and to strengthen the bargaining position respectively. On the other hand, 85% and 79% respondents either strongly agree or disagree that horizontal mergers are used to limit the competition and to have the consolidation effect respectively. There are more disagreements with regard to the motives or the outcomes of conglomerate mergers. A large majority either strongly disagree or agree that conglomerates diversify risk; they act as internal capital markets and are done to satisfy managerial motives.

In view of greater percent of negative statements relating to conglomerate mergers, it becomes necessary to identify why Indian firms go for conglomerate mergers. There exist a conflict in the results of Tables 5 and 7. According to Table 5, 90% of respondents view reducing the risk of existing business as the primary motive for mergers. Risk is reduced only through diversification which is accomplished by conglomerate mergers. However, only 34% of respondents view, as per Table 7, that conglomerate mergers are used to diversify risk. It can be surmised that even other mergers are done to smoothen earnings volatility.

**Table –8 Weighted Score**

(Weighted score = 4\*strongly agreed+3\*agreed+2\* disagreed +1\*strongly disagreed+0 \*can't say/10)

Sl. No.	Merger Motives	Weighted Score	Rank
1	Vertical mergers improve overall performance of merged firm	13.5	3
2	Vertical mergers strengthen a firm's bargaining position vis-à-vis suppliers and customers	16.5	1
3	Horizontal mergers limit the competition	14.9	2
4	Horizontal mergers produce consolidation effect on the industry	13.0	4
5	Conglomerates are used to diversify risk	9.4	8
6	Managers are poorer than shareholders	10.2	6
7	Horizontal and vertical mergers are more successful than conglomerates	9.9	7
8	A conglomerate works like a miniature capital market, reduces uncertainty and transaction cost	9.0	9
9	Conglomerate mergers are motivated by desire to build promotional opportunities for insiders	8.7	10
10	Conglomerates arise on account of industry clustering	10.6	5
	Mean	11.57	
	Standard Deviation	2.71	
	Variance	7.34	

Table 8 presents the weighted scores of the responses given by the respondents towards the various merger motives based on types of mergers. For vertical mergers strengthening of the bargaining position of the acquirer vis-à-vis the suppliers and customers appear to be the strong motive for mergers. On the other hand, limiting competition is the strong motives for horizontal mergers. Providing promotional opportunities for insiders and acting as internal capital market are regarded as the least important motives for conglomerates.

also influences merger financing. Cash compensation is taxable immediately on capital gains realized while stock financing postpones the tax liability to a future date. A firm signals manager's confidence and merger success through cash compensation while stock financing signals manager's lack of confidence and riskiness of the project. A highly levered firm uses equity stock for financing its mergers in view of lack of debt capital while a low levered firm may issue debt and use the cash compensation for financing firms.

### 6.6 Relationship between merger motives and method of financing

Mergers may be financed through cash, stock or combination of both. It is necessary to identify when a firm uses cash financing, stock, etc., and to test any sort of evidences on method of financing and merger motives. Factors affecting methods of financing are many and varied. A cash rich firm may use its excess cash to acquire firms while a cash poor firm may use its stock. Similarly, an overvalued firm may want to leverage its valuation and acquires firms using its overvalued stock (Shleifer and Vishny, 2004, Rhodes et al, 2005). Tax motive

In view of this significance between the merger motives and method of financing, the study enquires the Indian CEOs and CFOs on whether motives of mergers decide the method of financing. 3/4<sup>th</sup> of responding managers opine that motives and financing policies are interlinked.

### 6.7 Specific financing motives

The present study considers three specific financing motives, namely to deploy free cash flow, to issue overvalued stock and to signal manager's confidence level. Table 9 tabulates the relationship between these three motives:

**Table-9 Merger motives and method of financing**

Sl. No.	Merger motives	No of responses	(%)
A	To deploy free cash flow		
B	To issue overvalued shares to the target firm shareholders		
C	To signal manager's confidence level		
I	A only	06	12.50
II	B only	15	31.25
III	C only	--	--
IV	A and B	13	27.08
V	A and C	--	--
VI	B and C	--	--
VII	A, B and C	04	8.33
VIII	No Answer	10	20.83
IX	Total	48	100

Source: Compiled from primary data

Signalling manager's confidence level is not a motive for stock financing on its own in India. Only four sample companies have considered all these three factors in deciding on the method of financing. The large majority, 31%, have used overvalued stock to acquire cheap target while 27% have used the motive of deploying free cash flow and issue overvalued stock in selecting the method of financing.

### 6.8 Impact of Global Merger trends on Indian firms' merger motives

Changes in the World economy have universal effects irrespective of whether a country is developed or developing. The past experiences provide evidences in this regard. In recent years effects of these kinds of changes are very fast on account of globalization policy adopted by many countries. The economies of countries are more exposed to global economic developments. In view of this linkage, an attempt was made to enquire as to whether merger motives in India are related with the global merger trends. The study reveals that majority of managers of acquiring firms in India (52%) opine that global trends do not influence Indian mergers.

### 6.9 Role of Hubris Hypothesis in Indian Mergers

Mergers may be guided by managerial hubris, i.e., overconfidence, excessive pride,

ego or intuition. Acquiring firms even in the context of non-existence of merger benefits is explained to managerial hubris. Roll (1986) was the first to develop this hypothesis. A manager having this influence of hubris will acquire firms whether there are benefits or not. There is ample empirical support for managerial hubris. Overconfident managers feel that they have superior skills and are more competent than others. These cognitive biases motivate them to bet on their own judgment and engage in complicated tasks such as multiple acquisitions. Managers with overconfidence profiles tend to underestimate (overestimate) the risks (synergy gains) associated with mergers and are therefore less likely to postpone an acquisition decision. Overconfident managers are, in general, optimistic and predisposed to acquire targets quickly and frequently. Thus, overconfident managers are prone to engage in multiple acquisitions because they believe that such serial investment decisions are in the best interest of shareholders than "rational" managers do (Doukas and Petmezas, 2007).

We test the hubris hypothesis for Indian mergers by asking corporate managers whether they are guided by hubris, overconfidence or pride. Table 10 provides the response of the managers to the question.

**Table-10 Hubris hypothesis play a major role in merger selection**

Sl. No.	Opinion by respondents	No of responses	%
1	Yes	03	6.25
2	No	26	54.17
3	Unanswered	19	39.58
	Total	48	100.00

Source: Compiled from primary data

A perusal of Table shows that 54% managers opine in negative while only 6% opine that they were influenced hubris hypothesis. Nearly 40% of respondents remain unanswered. This can clearly mean Indian corporate mergers are uninfluenced by managerial hubris. There are several implications of these conclusions. It can mean that Indian managers always take appropriate or value maximizing mergers, which generate positive short-term announcement returns and positive long-run returns. However, the reality is otherwise. Indian mergers do generate negative short-term returns and there are negative returns even in the long-run.

## 7.0 Theoretical Justification for Indian Mergers

The study generates several hypotheses based on theoretical foundations of M&As. Weston et al (2006) classifies them into several groups as efficiency theories, agency problem and managerialism theory, free cash flow hypothesis, market power, redistribution, strategic perspectives, signalling hypothesis, etc. The objective is to test the applicability of these hypotheses to Indian context. Does M&A decision in India is taken to improve operational efficiency of combined firm as hypothesized by efficiency theories? Do Indian firms merge to resolve agency conflict or are a manifestation of the existence of agency problem? What is the extent of predictability of Indian mergers as per free cash flow hypothesis?

Table-11 tabulates the data relating to the opinions of respondent managers.

**Table – 11: Extent of Applicability for Merger Statements**

Sl. No.	Merger Hypotheses	Order of Preferences				
		1	2	3	4	5
1	Mergers are used to signal to the market	18 (38.90)	6 (12.76)	11 (23.4)	1 (2.13)	11 (23.40)
2	Mergers are manifestation of agency problem	12 (25.53)	4 (8.51)	13 (27.6)	1 (4.25)	16 (34.04)
3	Mergers resolve agency problem	15 (31.91)	3 (6.38)	13 (27.6)	3 (6.38)	13 (27.66)
4	Mergers are used to redistribute wealth among stakeholders	22 (46.81)	8 (17.02)	12 (25.5)	3 (6.38)	2 (4.25)
5	Mergers are guided by desire to use free cash flow	21 (44.68)	7 (14.89)	15 (31.9)	4 (8.51)	--
6	Mergers narrow strategic gaps in a firm	20 (42.55)	7 (14.89)	10 (21.2)	5 (10.63)	5 (10.63)
7	Mergers have no ulterior motives	16 (34.04)	5 (10.63)	16 (34.04)	4 (8.51)	6 (12.77)
8	Mergers improve the overall performance of acquiring firms	25 (53.19)	15 (41.91)	2 (4.25)	2 (4.25)	3 (6.38)
9	Mergers are done to circumvent loopholes in regulations	4 (8.51)	5 (10.63)	15 (31.91)	9 (19.14)	14 (29.79)

Source: Compiled from Primary Data

It seems Indian firms merge to improve overall performance as 85% of responding managers agree that mergers improve overall performance of acquiring firms. 59% agree that mergers are done to deploy free cash flows while 54% view that mergers lead to redistribution of wealth across various stakeholders.

There is no acceptance of the fact that mergers in India are a manifestation of agency

problem as 66% disagree with the statement. This could be attributed to the fact that large majority of Indian firms are family managed firms. Similarly, 81% do not regard mergers as mechanism to circumvent regulations.

Thus, it can be concluded that Indian mergers are guided by efficiency objective, free cash flow hypothesis, and to fill strategic gaps in the firm.



## 8.0 Conclusion

Corporate entities can achieve growth either internally or externally. M&As represent a form of external growth which enables firms to gain strategic advantage in a matter of few months. Mergers are considered as strategic decisions which allocate and reallocate resources across several industries and companies within an industry. In view of their strategic importance M&As have become popular among firms and are on the increase. The US has witnessed several mergers waves. Since liberalization, mergers are increasing.

Several explanations are given for the occurrence of M&A phenomenon. Efficiency theories, free cash flow hypothesis, hubris hypothesis, winner's curse hypothesis, redistribution, managerialism, etc., are some of the explanations extended to understand the occurrence of mergers. Present study aims to analyse motivations for Indian mergers of the period 2002-2010. A pre-tested questionnaire was circulated among the CEOs and CFOs for eliciting views relating to motives for corporate mergers. The survey reveals that the mergers are being regarded as strategic decisions by majority of responding managers in India. Obtaining synergistic gains from mergers has been the primary motive for merger with all the respondents agreeing to this motive followed by risk reduction through diversification. Motives such as to achieve personal ambition, to be the first among the competitors, to mimic merger decisions of competitive firms and to fall in line with the international mergers are the least rated motives.

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The motives of merger differ across types of mergers and mode of financing and Indian mergers are largely influenced by the desire to improve overall operational performance of the combined entity in both vertical and horizontal mergers. Risk reduction is the motive for conglomerate mergers but Indian firms diversify for reasons other than risk reduction. As far as method of financing is concerned, the Indian firms are primarily guided by the desire to use overvalued stock in acquiring undervalued firms. The deployment of free cash flow does not have takers in India. The study also reveals that Indian mergers are less influenced by the international merger waves.

Motives constitute an important aspect of merger process. Mergers should have an economic motive for them to contribute to the performance of firms. Mergers on grounds other than economic cannot be justified and bring benefits to managers only. By and large Indian mergers are guided by the desire to improve overall performance of combined entities. The reasons are far to seek. The Corporate India is structured around business families for several decades and is closely held. Mergers for non-economic reasons cannot be expected. The questions that remain unanswered are do mergers really improve operational efficiency and are these benefits distributed across all groups of shareholders.

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