ANALYSIS OF MERGERS AND ACQUISITIONS IN OIL AND GAS SECTOR IN INDIA AND ITS IMPACT ON OPERATING AND FINANCIAL PERFORMANCE

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Name of the Authors:

Alok Bhardwaj[1],
Kanchan Bisht [2],

[1]*Asst. Prof. JRE Group of Institutions, Greater Noida, UP (INDIA)*

[2] *PGDM Candidate, JRE Group of Institutions, Greater Noida, UP (INDIA)*

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ABSTRACT

Mergers and Acquisitions (M&A) are the most popular means of corporate restructuring. They have played a significant role in growth of number of leading companies in the world. Due to the deregulation of the Indian economy and recent economic reforms many International and domestic players have entered the Indian industries. This has lead to lot of corporate restructuring due to increasing competitive pressure. This paper focuses on studying the impact of Oil and Gas sector due to M&A by pre and post financial and operating indicators such as operating profit margin, PBIT margin, Net profit margin, ROA, RONW, ROCE, Investment Turnover ratio, Debtor turnover ratio etc. The paper studies the mentioned ratios of five major mergers and acquisitions activities happening in India from 2005 to 2015. The main objective of this paper is to find effect of merger and acquisitions (M&A) on the financial performance and operating performance of the acquiring firms in the post merger period. The study shows that there is no significant improvement in financial and operating performance of the companies due to mergers and acquisitions.

KEYWORDS:

Mergers and Acquisitions,

Oil and Gas,

India,

Financial,

Operating performance

INTRODUCTION

Mergers and Acquisitions (M&A) have played a very important role in the transformation in the Indian industrial sector. M&A activities increased after the Second World War period. The functional importance of M&As has undergone a sea change since liberalization in India. The MRTP act has been amended along with other legislations so as to assist large businesses and foreign companies to follow the M&A route for growthIn the post 2000 period we have witnessed a rise of M&A in India. The number and size of deals have become very big and it reached 1.3% of the global deal value in 2006.
So the reasons for all this are:

- Growth
- Need for reorganization within an industry to eliminate over-capacity
- Financial opportunities

CASES STUDIED:

In 2011, the acquisition of Abbot Point Coal Terminal, Australia was done by Adani Enterprises. This was the third overseas acquisition by the Adani Group. The deal size was also one of the largest amongst all port acquisitions in the world, and made the Adani Group the largest Indian investor in Australia.

GVK is one of largest power and infrastructure group of India, worth A$8bn bought two Australian coal mines from Hancock Prospecting which was privately controlled by the billionaire Gina Rinehart. GVK Power, part of the GVK Group, acquired Australia's Hancock Coal for $1.26 billion. GVK acquired majority holding in railways, coal resources, and port infrastructure projects of Hancock Coal. The company did long term contracts to supply 20 million tonnes of coal every year to support around 7,500 megawatts of power generating capacity.

Oil and Natural Gas Corp of India(ONGC) bought UK-listed Imperial Energy for £1.4bn ($2.6bn) which was its first acquisition of a foreign exploration and production company .The company aimed at securing foreign oil reserves and paid around £90m. Imperial had more than 6.8 billion barrels of oil equivalents in reserves. It was the biggest overseas acquisition by ONGC.

Coastal Gujarat Power Limited company was acquired by Tata enterprises in 2007.Coastal Gujarat Power Limited is a subsidiary of Tata Power Company Limited now. Coastal Gujarat Power Limited generates and sells electric power in Gujarat, India. Coastal Gujarat Power Ltd. Operates an ultra mega power project in Mundra which generates around 4000 mega watts of power. The company is based in Mumbai, India and was incorporated in 2006 .

Suzlon acquired the German wind turbine manufacturer Repower in 2007. This improved the company’s foothold in Europe.With the acquisition of REpower’s highly respected multi-megawatt class wind technology,

OIL AND GAS SECTOR IN INDIA

The oil and gas sector is an important industry in India and plays a vital role in decision making for all the other important sections of the economy. India was the third largest consumer of oil in the world in 2015. Oil imports constitute about 81% of India's total domestic oil consumption in 2015-16.This sector is one of 25 key areas under "Make in India" initiative. Natural gas was around 6.5% of the energy mix, in 2105.India has 230.066 MMTPA of refining capacity with a surplus refining capacity of 15%, making it the second largest refiner in Asia. India is the fourth largest LNG importer in 2015 with 6.4% of global imports.India held nearly 635 MMT of oil reserves in 2015in western part of the country. About 49% of reserves are onshore resources, while 51% are offshore.

A recent report indicatedthat the Indian oil and gas industry is anticipated to be worth US$ 139.8 billion by 2015. India’s economic growth is closely related to energy demand. It is projected that the need of oil and gas will grow in the future, therefore, investments in the sector are quite sensible.

The demand for oil and gas is increasing everyday and the Government has adopted several policies for the same.100% FDI has been allowed in many sectors including natural gas, petroleum products and refineries. India ranks fifth in LNG importers in the world. The country accounts for 5.5% of the world trade of LNG. In May 2016, the country imported 2.08 Billion Cubic Metres (BCM) of LNG witnessing a 43.38% YoY increase. The demand is expected to grow at a 16.89 % CAGR to 306.54 Million Metric Statndard Cubic Metres per Day (MMSCMD) by 2021.

FUTURE GROWTH IN OIL AND GAS SECTOR:

- Oil and gas sector plays significant role as it is one of the third energy required is met by the hydrocarbons.

- EIA projects India and China will show for about half of global energy demand growth through 2040, with energy demand of India is growing at 3.2% per year. As per BP Energy Outlook 2016, energy consumption of India is projected to grow at 4.2% per annum upto 2035.

- In 2016, country's natural gas pipeline network is spreaded over 14760.6 km. Another which is under various stages of implementation, 15000 km is received to complete national gas grid.

- New Domestic Gas Pricing guidelines is checking marketing freedom for difficult areas, and resolving other concerns in the existing areas under exploration and production have resulted into unlocking of reserves valued at Rs. 3.5 Lakh crore.

- There are other plans to connect 326 cities with city gas distribution network by 2022. The main concern is to promote use of natural gas, priority for allocation of domestic gas was accorded to PNG/CNG segments for meeting 100% demand and faster roll out of PNG connections and CNG stations.

- India's Refining capacity is forecasted to reach 256.55 MMTPA by 2020 after completion of the projects undertaken by refineries which are under process.

- The price of diesel has been made effective October 19, 2014, to provide better service delivery due to increased competition in the auto fuel sector. The saving in subsidy is been provided for funding anti-poverty and social sector schemes.

- The Government is focused on providing affordable, and modern energy to every person ,to promote clean cooking fuel. The planning is also going by government to increase LPG coverage by providing 10 crore new LPG connections in next 3 years till 2019.

- Under the scheme called Pradhan Mantri Ujjwala Scheme (PMUY), free connections of LPG are planned to be provided in next 3 years till 2019. It is being done to empower women of BPL families of 500 crore.

- LPG consumers are influence to voluntarily give up their LPG subsidy under 'GiveItUp' campaign. In june 2016, Against each `GiveItUp' consumer, more than 1.03 crore LPG consumers have given-up LPG subsidy .

- PAHAL launched for direct transfer of LPG subsidy to the bank accounts of LPG consumers which has resulted in right targeting of subsidy by elimination of 3.34 crore duplicate/inactive connections and saving of more than Rs. 21,000 crore of subsidy.

- A scheme called Direct benefit transfer of Kerosene (DBTK) is planned to launch for targeting of kerosene subsidy, would be launched initially in 40 selected cities across 9 States during 2016-17.

- The government has planned to roll out BS-IV auto-fuels from the country by April 1, 2017 and jump into BS-VI auto-fuels all over the country by April 1, 2020. It would help major investment in refinery upgradation, services sector ,auto industry,and related manufacturing .

LITERATURE REVIEW

A merger is the combination of two firms, where only one firm survives and assumes all the assets and obligations of the merged firm, which ceases to exist legally (Gaughan, 1999). Thus, mergers involve a consolidation process and the creation of a new firm with the dissolution of the original firms (Ross, Westerfield & Jaffe, 1998; Gaughan, 1999). Whereas, an acquisition relates to the transfer of ownership between two firms, where one firm (the acquirer) buys a part or the totality of another firm (the acquired) and establishes itself as the new owner (Ross et al.,1998).

In recent history numerous literature and papers have been researched on the impact of M&A on corporate capital consolidation and several theories have been proposed to understand the empirical validation of such impacts. Some of the effects that have been widely studied are the returns to shareholders following the merger and acquisition and the post-merger performance of the merged business entity. Following this, several measures have been postulated to understand and measure the performance of the company following M&A. These include the long and short term impacts of announcement, the effect of hostile takeovers etc. Mixed results were shown by Ikeda and Doi after they investigated the performance of the mergers of Japanese manufacturing firms using the measure of ROE and found that half the sample had their ROE increased post M&A and ROA increased in half the cases. However, over the 5 year period both these profitability measures showed an increase in more than half the firms, showing that there was a adjustment period where the acquiring firms learn to manage the new organisation. Kruse park and Suzuki examined the long term operating performance of Japanese companies where the sample used was 56 manufacturing organisations during the period 1966-97. This study showed a improvement of the operating performance over a 5 year period and that pre-merger and post-merger performance are highly correlated.

Research literature has shown us that the operating performance of the acquiring firms have shown mixed results in terms of the difference between the post-merger and pre-merger performance. Thus it would be extremely difficult to conclude whether the M&A can be use as a catalyst by acquiring firms to achieve better operating performance. Ramaswamy and Waegelein, 2003 tested the long-term post-merger financial performance of merged companies in Hong Kong to determine relationships between post-merger performance and firm size, the compensation plan, method of payment, and industry type. The analysis covered the five years pre and post-mergers (using operating cash flow returns on market value of assets as the measure of performance). The results have concluded that there is a positive significant improvement in the postmerger performance. Healy, Palepu, Ruback examined the performance of 50 US mergers post acquisition using.The criteria of cash flow performance and found that the operating performance of these companies were distinctly better following acquisitions. But the other claim that the operating cash flow performance did not improve following acquisitions was claimed by Ghosh in his paper. Kruse park and Suzuki examined the long term operating performance of Japanese companies where the sample used was 56 manufacturing organisations during the period 1966-97. This study showed a improvement of the operating performance over a 5 year period and that pre-merger and post-merger performance are highly correlated. Research literature has shown us that the operating performance of the acquiring firms have shown mixed results in terms of the difference between the post-merger and pre-merger performance. Thus it would be extremely difficult to conclude whether the M&A can be used as a catalyst by acquiring firms to achieve better operating performance.

Kaur,2002, compared the pre-merger and post-merger performance of acquiring companies using a set of financial ratio. The study concluded that profitability and efficiency declined post acquisition but there was no statistically different performance. However,Pawaskar who undertook the same study using firms during 1992-95 and ratios of profitability, growth, leverage and liquidity concluded that acquiring firms performed better then industry average in terms of profitability. When he performed a regression analysis, he found that to the contrary of earlier finding, there was no increase in post-merger profits compared to the industry average.

PramodMantravadi and A Vidyadhar Reddy analysed the post-merger performance of acquiring firm's different industries in India. The study found that there are minor variations in terms of impact on operating performance following mergers, in different industries in India. Empirical testing of post-merger performance of Indian companies has so far been proved inconclusive in order to derive any meaningful inference. The studies were also highly skewed in favour of a particular sector especially manufacturing ones and have a time period bias as only short time intervals were chosen to measure the performance. Ramakrishnan (2008), investigated that whether mergers in India have resulted in improved long-term post-merger firm operating performance through enhanced efficiency or not with the help of hypotheses. This study indicated that in the long run, mergers emerge to have been financially beneficial for firms in the Indian industry. Kumar,2009, examined the post-merger operating performance.The study attempts to identify synergies, if any, resulting from mergers. The study uses accounting data to examine merger related gains to the acquiring firms. It was found that the post-merger profitability, assets turnover and solvency of the acquiring companies, on an average, depicted no improvement when compared with pre-merger values. N. M. Leepsa& Chandra Sekhar Mishra (2012),in their research paper on "Post Merger Financial Performance: AStudy with Reference to Select ManufacturingCompanies in India",tries to study the trend in merger and acquisition (M&A) particularly with reference to manufacturing companies. The present study is an attempt to find out the difference in post-merger performance compared with pre-merger in terms of profitability, liquidity and solvency. The statistical tools used are descriptive statistics and paired sample t-test.

RESEARCH METHODOLOGY: -

Objectives of the study

- To study the effect of merger and acquisitions (M&A) on the financial performance of the acquiring firms in the post merger period.
- To study the effect of merger and acquisitions (M&A) on the operating performance of the acquiring firms in the post merger period.

Research hypothesis

Following hypotheses were formulated based upon the objectives:

- **H01:** There is no improvement in the financial performance of acquiring firms in post merger of Oil and Gas sector.
- **H02:** There is no improvement in the operating performance of acquiring firms in post merger of Oil and Gas sector.

Sample selection

The present study takes into account the Mergers in Oil and Gas sector announced between 2005 and 2015. We have compared pre-merger 1 year with post-merger years i.e. three years after merger has taken place. We have only taken companies into consideration where we can do comparison after 3 years of merger till 2015. Therefore, the sample was limited to merger announced before 2012.The sample size of study comes out to be 5mergers in the recent study period.

Statistical tools & techniques

Data has been analyzed using various sources.Also various statistical tools and techniques have been applied in this study. Mean, Variance and standarddeviation were used for descriptive statistics. The hypotheses are tested using Paired Sample t-test. SPSS and MS-Excel have been used to analyze data.

Data collection

Secondary sources have been used for data collection of various financial ratios for 1-year prior up to 3 years of post-merger of the sample companies which are: Moneycontrol.com and annual reports of the companies.

DATA ANALYSIS/HYPOTHESIS TESING

To analyze and test the hypothesis of one year pre merger(-1 year) and 3 year post merger(+1year),(+2year) and (+3 year) we have used " paired sample t-test" with confidence interval of 0.05 or 95% and descriptive analysis for mean difference. The results are showed in following table:

		Mean Value			T-Value			P-Value(2 Tailed)		
	-1	+1	+2	+3	-1,+1	-1,+2	-1,+3	-1,+1	-1,+2	-1,+3
1. Profitability standards										
Operating profit margin	0.72	0.742	0.54	1.164	-0.503	1.743	-0.488	0.641	0.156	0.651
PBIT margin	31.98	18.5	8.34	9.568	0.934	1.176	1.218	0.403	0.305	0.29
Cash profit margin	0.602	0.662	0.718	0.882	-0.87	-0.789	-1.13	0.434	0.474	0.322
Net profit margin	23.23	6.06	-8.55	-15.66	1.109	1.318	1.465	0.329	0.258	0.217
Return on Capital employed	11.25	8.86	9	4.9	0.783	0.7	0.982	0.477	0.523	0.382
Return on Net worth	13.69	12.242	9.984	10.98	0.374	0.47	0.327	0.734	0.671	0.765
Return on asset	8.27	5.95	3.97	2.93	1.359	1.003	0.962	0.246	0.373	0.391
2. Operating standards										
Inventory turnover ratio	18.48	9.56	12.31	10.57	1.022	0.895	0.983	0.382	0.437	0.398
Debtor turnover ratio	6.7	9.67	8.38	4.73	-0.126	0.047	4.539	0.906	0.965	0.011
Investment turnover ratio	1.04	0.45	1.98	4.06	1.578	-0.554	-0.986	0.19	0.609	0.38
Asset turnover ratio	47.08	34.85	38.37	31.12	1.484	1.544	1.778	0.212	0.197	0.15

Financial/Profitability ratios:

1) Merger has brought no change in operating profit post period (+1 year) p=0.641 >0.05. In comparison to pre-merger (-1 year) and post-merger (+ 2 year) p =0.156 > 0.05 still we can see there is no change in operating profit of the company. In comparison to pre-merger (-1 year) and post-merger (+ 3 year) p=0.651> 0.05 again in 3rd year there is no change in operating profit of the company.

2) There is no improvement in PBIT margin of the company (+1 year) p=0.403>0.05. In (+2 year) p= 0.305>0.05 again no change and improvement in PBIT margin. In (+3 year) p=0.290>0.05 again no change. So M&A doesn't improve PBIT margin of the company.

3) Cash profit margin of the company also has no change (+1 year) p= 0.434>0.05. In (+2 year) p=0.474>0.05 still no change in second consecutive year. In (+3 year) p=0.322>0.05, here also we can find in third consecutive year also there is no change in cash profit of the company.

4) M&A has not brought any change in Net profit of the company (+1 year) p=0.329>0.05. in (+2 year) p=0.258>0.05 still no improvement in second post year of M&A. In (+3 year) p=0.217>0.05 again M&A leads no change in net profit margin of the company.

5) Return on capital employed has also not improved by M&A as in (+1 year) p=0.471>0.05. In second consecutive year (+2 year) p=0.523>0.05 no improvement again. In third consecutive year (+3 year) p=0.382>0.05 still M&A is not able to get return on capital employed.

6) Return on net worth of the company hasn't received any significant improvement from M&A as in (+1 year) p =0.734>0.05. In (+2 year) p=0.672>0.05, no improvement can be seen. In (+3 year) p=0.671>0.05 again no significant improvement can be seen.

7) M&A also doesn't bring any improvement in Return on asset of the company as in (+1 year) p=0.246>0.05. In (+2 year) ROA leads to no improvement of the company p=0.373>0.05. In (+3 year) p=0.391>0.05 has no change in ROA of the company.

Operating ratios:

1) Inventory turnover ratio is also not affected in improvement by M&A as in (+1 Year) p=0.382>0.05. In (+2 year) p=0.437>0.05 still no change in company ITR. In (+3 year) p=0.398>0.05 again no improvement in ITR of the company.

2) M&A leads again no change in Debtor turnover ratio in (+1 year) p=0.906>0.05. In second consecutive year (+2 year) p=0.965>0.05 still it is showing no improvement. In third consecutive year(+3year) p=0.011<0.05 here we can see some changes and improvement in DTR.

3) Investment turnover ratio also doesn't has no significant changes by the effect of M&A as in (+1 year) p=0.190>0.05. In post second year (+2 year) p=0.609>0.05 still no improvement in the ratio. In post third year (+3 year) p=0.380>0.05, as we can see again M&A leads to no significant effect in investment turnover ratio of the company.

4) Asset turnover ratio of company has not improved significantly as in (+1 year) p=0.212>0.05. In post second year (+2year) p=0.1997>0.05, still no improvement in ATR of the company. In post third year (+ 3year) p=0.150>0.05, again no improvement caused by M&A in the company.

Hence, overall it can be said that Mergers and Acquisitions (M&A) in Oil and Gas sector leads to change in improvement of the company. Therefore, our null hypothesis(H0) was reliable and accepted and alternative hypothesis has been rejected(H1).

CONCLUSION

Mergers and Acquisitions (M&A) prime motive is to improve the value, wealth and growth of the enterprise but in the current case it is been observed that M&A has no effect on the company performance in Oil and Gas sector. It has been concluded that that there is no significant improvement in financial and operating standards in post-merger period. The results have been arrised from paired sample t-test at significant level of 95% which indicated that there is no significance difference in the defined financial performance standards between pre-merger and post-merger due to the significance value is greater than 0.05. Hence, this study has accepted the null hypotheses which consider that there are no significant improvements in surviving company's performance post-merger and acquisition and rejected the alternative hypothesis which considers that there is significance improvement in surviving company's performance post-merger and acquisition activity.

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