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"TAKEOVER OF FOREIGN COMPANIES BY TATA STEEL- AN ANALYSIS OF POST TAKEOVER PROFITABILITY "

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Abstract: The primary motive of each and every enterprise is to earn profit. In most cases, profit earning may be the major cause of takeovers. Profitability can be calculated from the profitability ratios which determine the company's overall efficiency and performance. The integration process of companies has a major impact on their profitability. During the current scenario of globalization and dogmatic competition takeovers has emerged out a much admired strategy to secure profits, continuous growth and added share value by gaining new resources, technological know-how, synergies, new markets and competitive advantage. Conversely, various studies reveal that takeover as a growth strategy provided both positive and negative consequences. Takeovers of Indian companies by Indian companies or foreign companies as well as takeovers of foreign companies by Indian companies are increasing quickly. Tata steel has done three cross-border takeovers in steel industry. The present study attempts to examine the pre and post takeover profitability of Tata Steel through paired t-test.

Keywords: Takeovers, Efficiency, Profitability.

INTRODUCTION

The current business environment is rapidly changing with respect to technology, markets, competition, products, people, process of manufacturing and consumers. The key challenges before any developing country is to cope with these changes, innovate its strategy and foster the economic growth. Strategic financial events like mergers, acquisitions and takeovers (M&A) are considered vital engines that help companies to grow in size, enter new markets, expand customer base, reduce competition, gain economies in scale, and technological know-how in respect to products, methods of manufacture and people as human capital. Academicians, eminent scholars and market analysts consider that takeover is a very effective inorganic strategy which prompts ways for a quicker widening and deepening of market and faster growth. Takeover refers to the act of a person or group of persons acquiring shares or voting rights or both of a company, from its shareholders, either through private negotiations with majority shareholders, or by a public offer in the open market with an intention to gain control over its management.

Thus, the term 'takeover' is a process whereby the majority of the voting capital of a company is bought through secret acquisition of shares or through a public offer to the shareholders. Takeover implies acquisition of control of a company which is already registered in any of the stock exchanges. Takeover is a business strategy of acquiring control over the management of the target company-either directly or indirectly. For attaining more profit and permanency in earnings, for best possible utilisation of financial, human and physical resources, for better economies of scale and profitability are also reasons behind takeover. Due to the various advantages it is found that in the present liberalised, privatised and globalised economic environment of India, takeovers have become very popular and are happening very frequently in almost every sector of the economy. The study aims to find out the impact of takeover on the profitability of Tata Steel.

Objectives of the Study:

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- To evaluate pre and post takeover profitability of Tata Steel.

Methodology:

The data has been collected from the secondary sources viz. annual reports of Tata Steel, journals, various websites etc. For comparing the pre and post takeover performance of Tata Steel, the study has used accounting and financial tools. Profitability ratios such as gross profit ratio, operating profit ratio, net profit ratio, return on investment, earnings per share and dividend per share have been considered under study. Paired t-test has been applied to evaluate the profitability of Tata Steel in pre and post takeover period.

Period and Scope of the Study:

The study aims to compare the profitability of Tata Steel in pre and post takeover period. Thus, the period of the study is taken from 2001-02 to 2009-10. The years 2004-05, 2005-06, 2006-07 and 2007-08 has been taken as "Cooling period", as the Tata Steel was busy in planning the takeover of three foreign companies, i.e. the NatSteel of Singapore in the year 2004-05, Millennium Steel of Thailand in the year 2005-06 and Corus of UK in the year 2007-08. Since during this period the Tata Steel was busy planning and executing the takeovers of foreign companies, the cooling period has not been touched for the analysis purpose. The study is confined to the cross-border takeovers i.e. takeover of Nat Steel, Millennium Steel and Corus done by Tata Steel.

Review of Literature:

Ravi Sanker and Rao K.V. (1998) analysed the implications of takeovers from the financial point of view with the help of certain parameters like liquidity, leverage, profitability etc. They observed that a sick company is taken over by a good management and makes serious attempts; it is possible to turnaround successfully.

Ali and Gupta (1999) found that the bidder firms in Malaysia have lower profitability, higher risk and lower leverage in comparison to other countries. The pre-takeover growth and profitability of the target firms was better than the control target firms comparison to other countries.

Coontz (2004) revealed that merger or acquisitions in the 15firms sample listed on the S&P 500 Index on an average decreases shareholders' wealth of the acquiring firm rather improving it.

Pazarskis, Vogiatzogloy, Christodoulou and Drogalas (2006) examined empirically the impact of mergers and acquisitions on the firms in Greece and found that the profitability of the firms decreases due to the mergers and acquisitions event.

Kumar (2009) enunciated that on average, the post merger and acquisition profitability and solvency of the acquiring firms shows negative results when compared with the pre merger and acquisition values.

An Overview of Tata Steel:

Tata Steel is one of the India's largest business conglomerates. The Tata Group established by Jamsetji Tata and his extended family. Tata Steel was founded in 1907, and the plant started production in 1912. At present, Tata Steel is India's largest steel maker and one of the worlds's most geographically diversified steel producer. Tata Steel is backed by 100 glorious years of experience in steel making; Tata Steel is the world's 5th largest steel making company with an existing annual crude steel production capacity of 30 Million Tonnes per Annum (MTPA). Tata Steel Group, with a turnover of US$ 24.82 billion in FY 2012- 2013, is a Fortune 500 company. Now a day's Tata Steel has a balanced global presence in over 50 markets and manufacturing operations in 26 countries. It has a shareholder base of over 800,000 people. It has employee strength over 81,000 across 5 continents. It produces different products like construction products, automotive products, aerospace products, consumer goods, material handling, energy and power sector related products, rail industry related products, engineering plant and equipments, agricultural tools, products for shipbuilding, packaging products, security and defence related products, etc.

Post Takeover Financial Performance of Tata Steel:

Profitability ratios consist of gross profit ratio, operating profit ratio, net profit ratio, return on investment, earning per share and dividend per share. The ratio measures the relationship between gross profit and net sales and is represented as a percentage. Operating profit ratio explains the relationship between operating profit and sales. Net profit ratio shows a relationship between net profit (after interest and tax) and sales. It indicates the efficiency of the management in manufacturing, selling, administrative and other activities of the firm. ROI establishes the relationship between net profit (after interest and tax) and shareholder's funds. It indicates the extent to which the primary objective of the firm i.e. to maximize its earnings is being achieved. EPS is an indicator of a company's ability to pay maximum amount of dividend per equity share. It establishes the relationship between net profit (after tax - preference dividend) and number of equity shares. DPS indicates the quantum of dividend distributed to each equity share.

All the ratios have been computed for three years before the takeovers and three years after the takeovers. The mean figures of profitability ratios and their standard deviations have been computed to apply the paired t-test. The fundamental purpose of applying t-test is to find out the approximate overall post takeover performance.

The mean figures of various profitability ratios and their standard deviations have been computed to app.ly the paired t-test. The basic purpose of applying t-test was to find out the approximate overall post takeover performance on the two groups of performance fronts.

The profitability ratios was tested for the Hypothesis (H0) that "there is no difference between mean profitability ratios in the pre takeover period and the mean profitability ratio in the post takeover period of the Tata Steel".

First, the profitability ratios have been analysed. Some of the profitability ratios have improved and some have deteriorated in post takeover period. To find out the overall approximate result of post takeover performance, paired t-test has been applied on the profitability ratios (taking various mean ratios together). The Hypothesis for the paired t-test is:

H0: There is no difference between pre takeover period mean and the post takeover period mean of the profitability ratio of the Tata Steel.

H1:There is difference between pre takeover period mean and post takeover period mean of the profitability ratio of the Tata Steel.

Profitability ratios	Pre mean	Post mean	d	d^2	n	DOF	S.D.	t value
Gross profit ratio	87.31	78.76	8.55	73.10	6	5	11.46	0.34
Operating profit ratio	58.02	54.46	3.56	12.67				
Net profit ratio	9.87	2.98	6.89	47.47				
ROI	25.04	11.48	13.56	183.87				
EPS	27.26	45.61	-18.35	336.72				
DPS	8.26	12.66	-4.40	19.36				
Total	215.76	206.05	Σd=9.81	Σd^2=673.19				

The result shows that the calculated value of t (0.34) is less than the tabulated value of t (2.57) at 0.05 level of significance at 5 degree of freedom. Thus, the Null Hypothesis is accepted. It means that there is no difference between the pre takeover period mean and post takeover period mean of the profitability ratio of Tata Steel. As such, the profitability of the Tata Steel in post takeover period has not improved and this belies the motivation for which the takeovers were done.

Conclusion:

The results show that in the post takeover period some of the individual performance dimensions have registered improvement and some others have deteriorated. In overall perspective, for the window period taken, there is no improvement in the financial performance the company. This is in line with the findings of various studies that have taken place in India and abroad. Research literature and previous studies that we have reviewed have shown us that the operating performance of the raider companies have shown mixed results in terms of the difference between the pre takeover and post takeover performance. Thus, it would be extremely difficult to conclude with definitive assertion that the mergers and takeovers can be or cannot be used as a strategic catalyst by a raiding or acquiring company to achieve a better operating performance in post takeover or post acquisition period.

One very important factor needs attention here that Tata Steel had resorted to massive borrowed capital for the takeover of the three foreign companies. This has resulted into an increase in financial leverage and the impact of the same is visible on the significantly improved EPS of the company in the post takeover period. But, what is worrying is that this has also resulted into deterioration of liquidity and solvency position of the company. The Tata Steel should take note of this situation and in view of the present gloomy and recessionary business environment and its dwindling interest coverage ratio, it should think of reducing the financial leverage.

It is observed from the analysis that in the last year of the post takeover period, performance of the Tata Steel registered significant improvement as various ratios for the company have become positive. This implies that the company's performance is improving and it gives an indication that the company is now stabilised and in years following the performance of the company will improve in line with the expectations with which the takeovers were done.

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