"Ovidius" University Annals, Economic Sciences Series
Volume XIX, Issue 2 /2019

Economic Performance in Merger Operations

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Abstract

The role of mergers has grown considerably in the new economic context. Since the end of the last century, the waves of mergers have raised different questions: Why are mergers occurring, what are the reasons? Does the merger generate the growth of the economic position and performance of the companies? Who benefits and who loses from the merger? Under the conditions of an increasingly competitive environment, the application of the best strategies by each company became imperative. The analysis of the financial performance has a determining role in establishing the strategy to be followed by the absorbing companies. The research hypothesis is: the merger operation has a positive impact on the financial position of the absorbing companies. Following the analysis of the financial position of the absorbing companies, it can be said that it is improving.

Key words: mergers, economic performance, shareholders
J.E.L. classification: G34, M21

1. Introduction

The activity of mergers and acquisitions is strongly influenced by the events in the global economic scene, which makes it difficult to make a forecast regarding the evolution of the merger activity in the medium and long term. In today's business environment there is a simple rule that applies to businesses: they either grow or disappear. Maintaining and improving the performance of companies during the period of mergers and acquisitions, with proper risk management, is a major challenge for businesses in the current business environment.

Regarding the performance of the merger operations, there is a great diversity of the results obtained. This fact is due to the diversity of the results of the samples used both in terms of geographical areas, analysis periods, types of operations, as well as in the sectors of activity. While some studies show that mergers lead to an increase in performance, others reveal a insignificant change or even a major deterioration in performance as a result of the merger transaction.

The analysis of the economic and accounting performance is done to compare before and after the external growth operation, starting from the evolution of the performance indicators. Among the most used indicators are the rate of economic return, the rate of financial return, the evolution of sales or market shares.

2. Literature review

Since the end of the last century, the waves of mergers have raised different questions: Why are mergers occurring, what are the reasons? Does the merger generate the growth of the economic position and performance of the companies? Who benefits and who loses from the merger? Given the wide range of those interested in the results of this process - namely, shareholders, managers, employees, consumers, society in general - a clear answer to this problem that satisfies all parties is unlikely to be given. Mergers are the main means by which companies can increase their activity and enter new markets, national enterprises becoming multinational companies.

Studies conducted on various companies have found that the first reason for mergers to occur is to increase the position and performance of the absorbing companies.

Table no. 1. Reasons for managers to perform mergers

Objectives for the realization of mergers	Answers (in%)
Increased financial performance and position	33 %
Increased market share and faster penetration in other markets	28 %
Acquisition of new technologies and skills	22 %
Elimination of competitors	11 %
Economies of scale	6 %

Source: Mantravadi and Reddy (2008, p.193)

Despite the popularity of the merger strategy, many of them do not produce the expected benefits. Although the benefits and costs of the merger have been frequently studied, controversies remain not only about the size of the net result of the companies but also about the sign, generating questions such as: Could a loss be recorded as a result of the merger? Do shareholders actually win? Previous empirical studies have investigated the impact of the merger on the financial position and performance of companies. These empirical studies can be divided into three groups: studies that reported a positive impact on position and performance, studies that reported a negative impact, and studies that did not find a significant impact on the performance of enterprises.

The latest US studies using more sophisticated techniques to measure changes in post-merger position and performance tend to show that they remain unchanged (Moeller, Schlingemann Stulz, Ghosh, 2004) or significantly improve after takeover (Heron, Lie, Linn, Switzer, 2002).

The findings of the UK studies are much more contradictory, with authors Dickerson, Gibson and Tsakalotos finding a significant decline in performance and post-merger position, while authors Powell and Stark show significant growth. Similar to UK studies, Asian studies also yield contradictory results. Empirical evidence shows that Japanese mergers have a negative impact on the financial position and performance of absorbing companies (Kruse, Park, Suzuki, 2013), Malaysian takeovers are associated with better post-merger financial performance and position (Rahman, Limmack, 2004), while mergers in Australia lead to insignificant changes in the profitability of the target company after taking over (Sharma, Ho, 1989).

For mainland Europe, researchers Gugler, Mueller, Yurtoglu and Zulehner point to a significant drop in sales but a significant increase in profit.

From the study of the specialized literature it is observed that the majority of the absorbing companies have performance before the operation of the forks. The authors Jensen and Ruback, Andrade, Mitchell and Stafford, Goergen and Renneboog or Campa and Hernando revealed, following the analysis of the stock market evolution, that those who earn the most from the mergers and acquisitions are the shareholders of the target companies, while the buyers seem to escape the "fingers" gain. Table 2 provides an overview of these studies.

Table no. 2. Overview of the empirical studies on the impact of the merger on performance

Authors	Dates	Country	Sample	Indicators	Grouping by
Studies that show an improvement in post-merger performance					
Powell, Stark (2005)	1985-1993	UK	191	ROE	Company size
Rahman, Limmack (2004)	1988-1992	Malaysia	113	Global financial economy ROE	Industry
Heron, Lie (2002)	1985-1997	USA	859	Net profit	Industry
Linn, Switzer (2001)	1967-1987	USA	413	Financial stability rate ROE	Industry
Parrino, Harris (1999)	1982-1987	USA	197	Net cash	Industry
Switzer (1996)	1967-1987	USA	324	Net cash Net profit ROE	Industry

Healy, Palepu, Ruback (1992)	1979-1984	USA	50	Gross Cash Flow	Industry
Moeller, Schlingemann (2004)	1985- 1995	USA	2.362	Liquidity rates, ROE	Industry
Gugler, Mueller, Yurtoglu,Zulehner (2003)	1981- 1998	Mondial	2.753	Sales income	Industry
Studies that did not find a significant impact on performance					
Sharma, Ho (2002)	1986-1991	Australia	36	Global debt ratio	Industry Company size
Ghosh (2001)	1981-1995	Global	315	ROE	Industry Company size
Herman, Lowenstei (1988)	1975-1983	USA	56	Net profit ROE	Ungrouping
Mueller (1980)	'50, '60, '70	Belgium, Germany, UK, USA, France, Holland, Sweden	different in the country	Profit net	Industry Company size
Lev, Mandelker (1972)	1952-1963	USA	69	Financial autonomy rate	Industry Company size
MartynovaOosting,Rennebo (2006)	1997-2001	Europe	155	Profit net EBIT	Industry
Studies that show a deterioration of the post-merger performance					
Kruse,Park Suzuki (2002)	1969-1992	Japan	46	Cash net	Industry Company size
Yeh, Hoshino (2001)	1970-1994	Japan	86	Financial working fund	Industry
Dickerson, Gibson, Tsakalotos (1997)	1948-1977	UK	1.443	General solvency rate	Industry
Clark,Ofek (1994)	1981-1988	USA	38	EBIT	Industry
Meeks (1977)	1964-1972	UK	223	Gross profit	Industry
Hogarty (1970)	1953-1964	USA	43	EPS	Industry

Source: own processing

The results of previous empirical studies are inconsistent because their position and financial performance cannot be measured from a single indicator, and the results are different although many of them have been performed in the same geographical regions and for comparable time periods.

3. Research methodology

The research approach has an empirical character, proposing to validate its working hypotheses through a deductive-inductive process. The study uses methods specific to the quantitative (positivist) approach.

3.1. Purpose and objectives of the research

In the research I started from the finding that, regarding the reasons for the merger, the first place is the improvement of the financial position and the performances of the absorbing company or the companies involved.. Table no.3 allows to establish a hierarchy of the reasons that determine the companies to resort to the merger, as a reorganization strategy.

Table no. 3. The reasons for the merger in Romania

Mergers motives	Percent
Increased financial position and performance	76 %
Increasing market share	60%
Simplifying the decision-making process and reducing administrative costs	55%
Increasing sales capacity	30%
Increased bargaining power with suppliers, customers	10%
Better allocation of resources	15%
Better use of existing facilities and workforce	15%

Source: own processing

Given the fact that in the top of the preferences of the Romanian companies that resort to the merger is the reason for the improvement of the performances and the financial position and that the studies undertaken at international level have led to different conclusions, we propose to analyze whether the mergers in our country of the last period have achieved this objective.

Given our research approach, we resorted to establishing the following hypotheses::

Hypothesis 1: The merger operation has a positive impact on the financial position of the absorbing companies;

Hypothesis 2: The merger operation has a negative impact on the financial position of the absorbing companies.

3.2. Population and sample

The target population used in the analysis is as follows: Companies listed on the Bucharest Stock Exchange. The sample analyzed: 61 companies; the criterion taken into account - absorbing companies that have the merger project published in the Official Gazette of Romania, part IV during the period 2017-2018.

Data source: Central University Library Iasi, where I consulted the Official Gazette of Romania part IV. Information: collection from the merger projects by absorption of the companies data from the merger financial statements.

The analysis was carried out for two years: one year before the merger and one year after the merger.

Analysis tools and procedures: data collection by observation method, data sorting and grouping, tables, graphs. The study is based on the method of economic-financial analysis that contains a set of methodological steps and procedures to establish and quantify the causal relationships between the studied indicators and the determinants: comparison of financial statements, analysis by rates (Ratios), use of the computer tool for data storage, calculating rates, determining financial balances, determining the evolution in time and space of the indicators.

4. Findings

In order to ensure the comparability of the data, we resorted to identifying the evaluation method used by the companies involved in the merger process in Romania during the analyzed period.

Table no. 4. The valuation method used by Romanian companies

	Frequencies
Valid	
Updated cash flow method	5
The patrimonial method	56
Method of comparison	0
Total	61

Source: own processing using the SPSS 19.0 statistical program

Thus, out of the 61 absorbing companies, we used to analyze the impact of the merger on the financial position and the performance of the entities, the 56 companies that used the patrimonial valuation method.

Before proceeding to the actual analysis of the impact of the merger on the financial position of the analyzed entities, we propose to present a situation of the changes undergone by the structure rates of the assets and liabilities positions for the 56 analyzed companies.

Table no. 5. The evolution of the structure rates of the assets by domains

Changes in the rate of fixed assets after the merger						
					Industry	Total
	Commerce	Production	Services	Financial service	Transport	
Number of companies where the indicator decreased	6	5	4	3	3	21
Number of companies where the indicator has grown	13	9	5	6	3	34
Total	19	14	9	8	6	56
Changing the stock rate after the merger						
					Industry	Total
	Commerce	Production	Services	Financial service	Transport	
Number of companies where the indicator decreased	10	6	8	5	3	32
Number of companies where the indicator has grown	8	9	4	2	1	24
Total	18	15	12	7	4	56
Changing the rate of money availability after the merger						
					Industry	Total
	Commerce	Production	Services	Financial service	Transport	
Number of companies where the indicator decreased	8	6	5	2	1	22
Number of companies where the indicator has grown	11	8	7	6	2	34
Total	19	14	12	8	3	56
Changing the debt ratio after the merger						
					Industry	Total
	Commerce	Production	Services	Financial service	Transport	
Number of companies where the indicator decreased	14	11	10	5	2	43
Number of companies where the indicator has grown	6	3	2	2	1	13
Total	20	14	12	7	3	56
Changing the rate of current assets after the merger						
					Industry	Total
	Commerce	Production	Services	Financial service	Transport	
Number of companies where the indicator decreased	13	9	4	3	2	31
Number of companies where the indicator has grown	6	6	8	4	1	25
Total	19	15	12	7	3	56

Source: own processing

Regarding the rate of fixed assets, it is observed that most of the absorbing companies have registered an increase. In most of the absorbing companies, the rate of inventories decreased. In terms of the availability rate, most companies have registered an increase and the Debt rate has decreased for most companies.

Most companies recorded a decrease in the rate of current assets.

As a general observation, all the companies with significant changes in the structure rates of the asset are in the trade field.

Table no. 6. The evolution of the structure rates of the liabilities by domains

Changing the share of equity in total liabilities					
		Number of companies to which the indicator			total
		Decreases	Does not change	Increases	
Industry	Commerce	5	0	17	22
	Production	4	0	7	11
	Services	4	1	5	9
	Financial services	2	0	8	10
	Transport	1	0	3	4
Total		12	1	43	56
Modificarea ponderii capitalului permanent în total pasiv					
		Number of companies to which the indicator			total
		Decrease	Increase		
Industry	Commerce	7	12		19
	Production	5	10		15
	Services	4	8		12
	Financial services	1	5		6
	Transport	0	4		4
Total		18	38		56
Changing the share of long-term liabilities in total liabilities					
Count					
		Number of companies to which the indicator			Total
		Decreases	Does not change	Increases	
Industry	Commerce	3	9	7	19
	Production	4	8	2	14
	Services	3	7	2	12
	Financial services	2	4	1	7
	Transport	1	3	0	4
Total		13	35	8	56
Changing the weight of short-term liabilities in total liabilities					
		Number of companies to which the indicator			Total
		Decrease	Increase		
Industry	Commerce	13	7		20
	Production	9	6		15
	Services	8	5		13
	Financial services	5	2		7
	Transport	1	0		1
Total		36	20		56

Source: own processing

Regarding the share of equity in total liabilities, it is noted that most of the absorbing companies have registered an increase. The share of permanent capital in total liabilities registered an increase in most absorbing companies.

Regarding long-term debt, it is noted that their share in total liabilities, in most companies does not change.

As a general observation, all the companies with significant changes in the structure rates of the asset are in the trade field.

Starting from the values of the balance sheet items for the analyzed companies, we proceeded to determine average values of the structure indicators, values that are presented in the following table.

Table no. 7. The evolution of the value of the financial position after the m

Indicators	Values before merger	Value after merger	Explanations
Rate of fixed assets	61%	53%	Rai=Ai/At
Accepted value	60%	60%	MAXIM
Index of growth of fixed assets	100%	114	$Ai=Ain/Ai_0$
Growth index of total assets	100%	127%	$At=Atn/At_0$
Turnover growth index	100%	206%	$CA=Can/Ca_0$
Rate of current assets	36%	43%	Rac=Ac/At
Accepted value	40%	40%	Maxim
Growth index of current assets	100%	149%	Ac=Acn/Ac0
Debt rate	8%	14%	Rcr=Cr/At
Debt growth index	100%	249%	Cr=Crn/Cr0
Availability rate	1,3%	2,1%	Rdp=Dp/At
Accepted value	2%	2%	Maxim
Availability growth index	100%	218%	Dp=Dpn/Dp0
Financial stability rate	39%	59%	Rsf=Cpm/Pt
Mimimum value	50%	50%	Minim
Equity growth rate	100%	183%	Cpm=Cpmn/Cp0
Growth rate of total liabilities	100%	139%	Pt=Ptn/Pt0
Rate of global financial autonomy	25%	12%	Rat=Cpr/Pt
Minimum value	33%	33%	Minim
Global debt ratio	72%	67%	Rig=Dt/Pt
Maximum value	66%	66%	Maxim
Growth index of total Debt	100%	115%	Dt=Dtn/Dt
Term borrowing rate	37%	43%	Rit=ÎTML-Cpm
Maximum value	50%	50%	Maxim
Growth rate of medium and long-term loans	100%	267%	ITML=ITMLn/ITML0

Source: own processing

The debt rate increases as a result of the merger, its pace exceeding the increase in turnover, which means an average duration of large and increasing receivables, will adversely affect the revenues of the company. However, the increase in the debt ratio following the merger is a favorable aspect because it is due to the increases in the availability. The availability rate shows the weight of the most liquid assets in total assets, that is the immediate liquidity degree of the current assets. The decrease in the volume of sales, the drastic decrease in the demand for products and services, the decrease of population incomes, the reduction of the number of jobs, very high increases of prices for raw materials, utilities and food, inflation, large variations of the exchange rate and the financial blockade generated by the receipts delayed caused the reduction of the availability of companies.

The availability rate improves as a result of the merger. The savings resulting from the common use of the equipment, the cost of production, the elimination of duplicate activities, the transfer of knowledge, etc. have led to an increase in the availability of companies. The turnover growth index exceeds after the merger the index of availability increases, which means an increase of the receipts compared to the payments made and a higher speed of rotation of the current assets, with possibilities of increasing the results. The financial stability rate reflects the extent to which the company has permanent financial resources against the total liabilities. The prevalence of permanent capital in the total financial resources of the company confers a high degree of security through stability in financing. Deposits of companies below the 50% led businesses to use debt to finance current activities. Prior to the merger, the companies were characterized by an increased insolvency risk due to over-indebtedness.

The term debt ratio reflects the extent to which medium- and long-term loans participate in the formation of permanent resources. The condition that must be met is that the term debt ratio, calculated according to this formula, is less than 50%. The level of this rate is important for businesses in financial policy making and financial institutions when assessing an application for new credit from the company.

5. Conclusions

Claims rate increase following the merger, its pace exceeding the growth in turnover, which means an average Receivable large and growing, which will adversely affect the company's earnings. The turnover growth index exceeds after the merger the index of availability increases, which means an increase of the receipts compared to the payments made and a higher speed of rotation of the current assets, with possibilities of increasing the results. The preponderance of permanent capital in total liabilities confers a high degree of financial security. Net working capital growing and positive shows that all fixed assets are financed from permanent capital, which represents a favorable situation for companies The need for working capital increases after the merger operation, so the company has current assets that are financed from permanent resources.

The ability of firms to meet their short-term obligations from current assets as well as from availability, increases as a result of the merger. The share capital covers the obligations to creditors and shareholders following the merger, which gives an optimum degree of solvency.

Permanent capitals regain their initial monetary form 12 days faster after the merger. As a result of the merger, the stocks recover their original money form in a much shorter time, by 49 days. The companies collect the value of the goods from the customers 15 days faster after the merger. The term of payment of the debts to the suppliers expires after the merger and is approaching the normal limit of 30 days.

Thus, the causes of the merger of the Romanian companies were: decrease of the volume of sales; decrease of population incomes; rising unemployment; rising inflation; large variations in the exchange rate; very large increases in prices for raw materials, utilities; sharp decline in demand for products or services; decrease of the cash availability of the enterprises; suprațndatorarea; increase of debts to providers, employees and social insurance budget; late payments of receivables.

Among the effects of the merger operation on Romanian companies, we note: obtaining economies of scale; increasing the bargaining power with suppliers, which leads to lower prices for raw materials, utilities; increasing availability; short-term debt relief; financing the activity from own resources; increasing financial stability; reducing the total debt and reducing the risk of insolvency; recovering debts from turnover in 238 days faster; recovering the value of the stocks in 48 days faster; debt recovery 25 days faster; financial release.

As a conclusion regarding the impact of the merger on the financial position of the absorbing companies, it can be said that it is improving.

6. Acknowledgement

This work was supported by a grant of the « Alexandru Ioan Cuza » University of Iasi, within the Research Grants program, Grant UAIC, code GI-UAIC-2018-05.

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