Company performance before and after a merger

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Abstract- This study aims to compare the financial performance of non-finance companies listed on the Indonesia Stock Exchange for the period 2010-2014 before and after a merger and acquisition. This study used the long-term pre and post-merger financial data to investigate the long-term performance. The present work conducted a comprehensive ratio analysis of 14 major ratios related to profitability, efficiency, leverage, and liquidity. The method used in testing the research was a quantitative approach with paired t-test and Wilcoxon test. The results of this study show that financial performance after the merger and acquisition (M&A) was better than before.

Keywords: financial performance, ratio analysis, merger and acquisition

1 INTRODUCTION

Industries are becoming more competitive in developing strategies to survive and grow in this globalization era. Every company chooses the best strategy to win the competition and survive in the future. One of the strategies for a company to survive the competition is by doing a business expansion. (Lesmana & Gunardi, 2012).

Business expansion strategy can be done in two ways, namely internal expansion, which is developing the company without involving any outside organization, and external expansion strategy, which is developing the company by involving outside organizations or companies such as by merger and acquisition.

Merger and acquisition (M&A) has been applied in Indonesia since the enactment of Law Number 1 of 1995 concerning Limited Liability Company. M&A has increased in several countries such as Turkey (Selcuk & Yilmaz, 2011), China (Yan & Ming, 2011), and India (Kumara & Satyanarayana, 2013; Rani *et. al*. 2015). M&A is a choice for companies around the world in order to maintain and achieve the target growth.

Theoretically, M&A is conducted by companies in order to improve the financial performance. However, the improvement of financial performance does not always happen in the companies who perform M&A. Several studies showed that the financial performance after M&A does not show a significant difference. In fact, some companies experience lower financial performance after M&A.

The result of the study conducted by Rani *et al*. (2015) on the comparison of company performance before and after M&A in India shows that after performing M&A, the average of ROE, ROCE, OPM_S, OPM_A, NPM, COGR, LRE, and FATR were increasing while SRE, RDE, TATR, and CATR were decreasing. The overall result shows that the financial performance of the companies in India experienced an improvement after M&A.

Andati *et al*. (2015) conducted a research on the comparison of the plantation company performance before and after M&A. The result shows that after performing M&A, the average of DER and EVA were increasing while ROA, ROE and PBV were decreasing. In other words, M&A did not show improvement of the company financial performance.

2 RESEARCH METHODS

The data were the financial report data which had been continuously audited every year within the 2007–2017 period of the entire non-finance sector companies listed in Indonesia Stock Exchange (IDX) within the 2010-2014 period that performed M&A. The time limit for assessing the companies' financial performance was five years, from 2010 to 2014. The time sample used was three years before and three years after performing M&A. The collected data were then processed using Microsoft Excel and SPSS 23 software for Windows. The data were used to measure the comparison of financial performance before and after the M&A. The analysis technique used was inferential statistic method because this method was for answering the hypothesis.

3 RESULT AND DISCUSSIONS

There were 29 companies chosen to be the sample for this study. Those companies performed M&A in the following year: one company performed M&A in 2010, six companies in 2011, six companies in 2012, nine companies in 2013, and seven companies in 2014.

Table 1. The Result of Profitability Ratio Test

Pair sample		t-stat	asymp sig	Conclusion
ROCE	(-1,+1)	-2.692***	0.007	significant
	(-1,+2)	-3.795***	0.000	significant
	(-1,+3)	2.912***	0.007	significant
	(-2,+2)	-3.189***	0.001	significant
	(-3,+3)	-3.816***	0.000	significant
ROE	(-1,+1)	-2.411	0.016	insignificant
	(-1,+2)	-3.860***	0.000	significant
	(-1,+3)	-4.141***	0.000	significant
	(-2,+2)	2.912***	0.007	significant
	(-3,+3)	-3.189***	0.001	significant
OPMs	(-1,+1)	-0.789	0.430	insignificant
	(-1,+2)	-1.287	0.198	insignificant
	(-1,+3)	-3.146***	0.002	significant
	(-2,+2)	-1.438	0.150	insignificant
	(-3,+3)	-2.519	0.012	insignificant
OPMa	(-1,+1)	2.173***	0.030	significant
	(-1,+2)	-2.649***	0.008	significant
	(-1,+3)	-3.103***	0.002	significant
	(-2,+2)	-2.692***	0.007	significant
	(-3,+3)	-3.038***	0.002	significant
NPM	(-1,+1)	-1.870*	0.061	significant
	(-1,+2)	-2.584***	0.010	significant
	(-1,+3)	-4.011***	0.000	significant
	(-2,+2)	-2.584***	0.010	significant
	(-3,+3)	-2.908***	0.004	significant

Note: *,**,and *** significant at 10%, 5% and 1%.

The overall results of the ROCE test show that the company performance after M&A was bigger than before M&A. A better ROCE after M&A shows that the company had used the capital effectively to generate profitability. According to Rani et al. (2015), this increase in performance could be related to M&A. The increase of effectiveness in the utilization of fixed assets by the company that was acquiring resulted in higher operating profits.

The ROE results also show that the overall performance of the company after M&A was greater than before M&A, and only ROE (-1, + 1) was not significant. In the early period after M&A, the company had not been able to use its capital effectively to generate profits. Paymata & Setiawan (2004) explained that the merger and acquisition process required a relatively large amount of money and capital, so the company had not been able to optimally utilize its own capital to generate maximum profit. Companies could use their capital optimally to generate profits for a period of 2 years and 3 years after M&A. Andati et al. (2015) found that there was a strong relationship between the level of leverage and company performance. The level of leverage was positively correlated with performance. The decreasing leverage levels after M&A also resulted in a decrease in profitability and firm value. This study also found an increase in leverage and profitability.

The OPM results show that the company performance after M&A was not necessarily greater than before performing M&A, which was (-1, + 3). Larger company size after performing M&A, would not necessarily increase the company's operating profit too. It was because new companies were joining resulting in the increasing operating expenses. Paymata & Setiawan (2004) stated that the company was focusing more on adjusting work culture after performing M&A. Employees who worked in companies needed a long time to be able to adjust to the new environment, so it could affect company performance. Rani et al. (2015) mentioned that a significant post-M&A operating margin indicated that the acquirers appear to have generated higher operating profit per net sales unit after the M&A. A better operating margin seemed to be caused by a decrease in costs as a result of economies of scale.

The NPM results show that company performance after M&A was greater than before M&A. This shows that the net income generated from sales after M&A was better than before M&A. Rani et al. (2015) proved that better margins in the post-M&A period show managerial ability to realize the expected synergy so that profitability became better.

Table 2. The Result of Weight Ratio Test

Pair sample		Z-stat	asymp.sig	Conclusion
COGR	(-1,+1)	-1.361	0.184	insignificant
	(-1,+2)	-0.461	0.649	insignificant
	(-1,+3)	-1.676*	0.094	significant
	(-2,+2)	-0.377	0.709	insignificant
	(-3,+3)	-0.508	0.611	insignificant
LRE	(-1,+1)	-2.087**	0.037	significant
	(-1,+2)	-1.546	0.122	insignificant
	(-1,+3)	-2.497	0.013	insignificant
	(-2,+2)	-0.616	0.538	insignificant
	(-3,+3)	-1.395	0.163	insignificant
SGR	(-1,+1)	-1.957**	0.050	significant
	(-1,+2)	-1.784*	0.074	significant
	(-1,+3)	-2.670***	0.008	significant
	(-2,+2)	-0.876	0.381	insignificant
	(-3,+3)	-1.676*	0.094	significant
RDE	(-1,+1)	-1.461	0.144	insignificant
	(-1,+2)	-0.365	0.715	insignificant
	(-1,+3)	-1.826*	0.068	significant
	(-2,+2)	-0.365	0.715	insignificant
	(-3,+3)	-1.826*	0.068	significant

Note: *,**, and *** significant at 10%, 5%, and 1%.

The COGR results show that the performance of the company after M&A was not necessarily greater than before M&A unless the pair of variables COGR (-1, + 3) shows significant results. This shows that the company had not been efficient in using funds for operational expenses. Rani et al. (2015) stated the economies of scale realized after M&A and the high volume of raw materials. Significant COGR results indicated that acquirer companies had achieved an operational economy from their production costs.

The LRE results show that the performance of the company after M&A was not necessarily greater than before M&A except for the variable pairs LRE (-1, + 1). Funds for labor were increasing because of the larger size of the company causing the increase in future expenses, including the labor cost. Rani et al. (2015) also gave the same results. Significant LRE results show that the company had realized the synergistic benefits of M&A by controlling costs, especially costs related to labor.

SGR results show that the performance of a company after M&A was not necessarily greater than before M&A except for the variable pairs SGR (-2, + 2). This shows that after M&A, the use of funds from sales used for sales, general and administrative expenses increased. It means that after M&A the company had been effective in using funds for sales, general and administrative expenses from sales. Acquiring companies had reached the economy in sales, general and administrative costs (Rani et.al, 2015). The insignificant results in SGR were likely due to the marketing economy realized after M&A. Higher sales volume and advertising costs might be the reason.

RDE results show that the company's performance after M&A was not necessarily greater than before M&A except for pairs of RDE (-1, + 3) and (-3, + 3) variables. This shows that after three years of conducting M&A, the company had been more effective in using funds for research and development. Paymata and Setiawan (2004) mentioned that employees who work in companies need a long time to be able to adjust to the new environment so that they can affect company performance.

Table 3. The Result of Activity Ratio Test

Pair sample		Z-stat	asymp.sig	Conclusion
FATR	(-1,+1)	-0.270	0.787	insignificant
	(-1,+2)	-1.373	0.170	insignificant
	(-1,+3)	-2.411	0.016	insignificant
	(-2,+2)	-1.806*	0.071	significant
	(-3,+3)	-2.000**	0.045	significant
CATR	(-1,+1)	-0.941	0.347	insignificant
	(-1,+2)	-1.222	0.222	insignificant
	(-1,+3)	-1.027	0.304	insignificant
	(-2,+2)	-1.200	0.230	insignificant
	(-3,+3)	-0.681	0.496	insignificant
TATR	(-1,+1)	-3.341***	0.001	significant
	(-1,+2)	-3.362***	0.001	significant
	(-1,+3)	--3.795***	0.000	significant
	(-2,+2)	-3.773***	0.000	significant
	(-3,+3)	-3.860***	0.000	significant

Note: *,**,and *** significant at 10%, 5% and 1%.

CATR results show that the company's performance after M&A was not necessarily greater than before M&A. This shows that after performing M&A, the effectiveness of the company in using current assets to generate income was not better than before M&A. Rani et al. (2015) proved that the low turnover ratio in the post-M&A period indicated unemployment capacity and lack of utilization of available resources.

TATR results show that company performance after M&A was greater than before performing M&A. This shows that after performing M&A, the effectiveness of the company in using its total assets to generate income was better than before M&A. Rani et al. (2015) show that the high turnover ratio in the post-M&A period was an indication of a better use of available resources.

Table 4. The Result of Debt Ratio Test

Pair sample		Z-stat	asymp.sig	Conclusion
DR	(-1,+1)	-2.065**	0.039	significant
	(-1,+2)	-2.238**	0.025	significant
	(-1,+3)	-2.238**	0.025	significant
	(-2,+2)	-2.022**	0.043	significant
	(-3,+3)	-1.697*	0.090	significant

Note: *,**,and *** significant at 10%, 5% and 1%.

The DR results show that the company's performance after M&A was greater than before M&A. This shows that company assets obtained from debt were greater than M&A. Andati et.al (2015) shows that there was a strong relationship between the level of leverage and company performance. The level of leverage was positively correlated with performance. Decreasing the level of leverage after mergers and acquisitions also resulted in a decrease in profitability and corporate value. What happened in this study was an increase in leverage and increased profitability.

Table 5. The Result of Liquidity Ratio Test

Pair sample		Z-stat	asymp.sig	Conclusion
CR	(-1,+1)	1.660	0.108	insignificant
	(-1,+2)	1.278	0.212	insignificant
	(-1,+3)	1.458	0.156	insignificant
	(-2,+2)	1.162	0.255	insignificant
	(-3,+3)	1.516	0.141	insignificant

Note: *,**,and *** significant at 10%, 5% and 1%.

The CR results indicate that the company's performance after M&A was not necessarily greater than before M&A. This shows that the ability of the company's current assets in meeting short-term obligations was not necessarily greater after M&A. CR which was not necessarily bigger after mergers and acquisitions (M&A) shows that the company wanted to maintain the liquidity of its company. Hanantyo (2017) stated that current liabilities and current assets tend to be constant every year despite the acquisition. There was no significant increase or decrease in the period before and after the acquisition. The acquisition should mean that the company's current assets were combined so that the company's ability to fulfill its short-term obligations should be better.

4 CONCLUSION

In this study, profitability ratios and debt ratios show better financial performance after mergers and acquisitions (M&A) than before mergers and acquisitions (M&A). Thus, in terms of profitability ratios, the company had achieved the desired synergy of merger and acquisition strategies (M&A). On the other hand, the ratio of expenses, activities, and liquidity, financial performance were not better after mergers and acquisitions (M&A) than before mergers and acquisitions (M&A). However, the company's financial performance of the company in general after the merger and acquisitions (M&A) was better than before mergers and acquisitions (M & A).

Things that might cause financial performance becoming less optimal were adjustments to the new organizational culture, selection of target companies, and poor use of resources. This research used analysis for 3 years before and after mergers and acquisitions (M & A) as a comparison of its financial performance. The strategy of mergers and acquisitions (M & A) was carried out for the long term, so the research should also be conducted with a longer term such as 5 years.

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