EFFECTIVENESS OF PROFITABILITY PERFORMANCE OF SELECT FMCG COMPANIES DURING THE PRE AND POST MERGER PERIOD

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Received: September 08, 2018 Accepted: October 31, 2018

ABSTRACT: *Fast moving consumer goods (FMCGs) constitute a large part of consumers' budget in all countries. The purpose of this paper is to investigate the relationship between pre and post-merger firm's profitability and to identify the variables that most affect profitability. It is considered to be a vital issue in financial management decision and it has its effect on liquidity as well as on profitability of the firm. Moreover, an optimal level positively contributes in creating firm value. In this study, a sample of 3 FMCG (Fast Moving Consumer Goods) companies in India from CMIE database covering a period of 3 years. Profitability has been measured in terms of net profit ratio, return on capital employed ratio, return on assets, return on net worth, earnings per share ratio have been used as explanatory variables. This article includes introduction, review of literature, analysis and interpretation, findings, suggestions and conclusion.*

Key Words: *Profitability, Merger and Acquisition, FMCG, Ratio Analysis.*

1.1 INTRODUCTION

The primary objective of a business undertaking is to earn profit. Profit earning is considered to be essential for the survival of any business. In the words of Lord Keynes, "profit is the engine that drives the business enterprise". A business needs profit not only for its existence but also for expansion and diversification. The investors want an adequate return on their investments, the workers want higher wages, creditors want higher security for their interest and loan and so on. A business enterprise can discharge its obligation to the various segments of the society only through earning profit. Profits are, thus, a useful measure of the overall efficiency of a business. Profits to the management are the test of efficiency and the measurement of control; to owners, a measure of worth of their investment; to the creditors, the margin of safety; to employees, a source of fringe benefits; to governments, a measure of tax-paying capacity and the basis of legislative action; to consumers, a hint to demand for better quality and price cuts; to an enterprise, less cumbersome source of finance for growth and existence and finally, to the country profits are an index of economic progress. Profitability ratios are calculated to measure the overall efficiency of the business. Thus an attempt was made to analyze the profitability position of the company. The following are the ratios used to measure the profitability: Net Profit Ratio, Return on Capital Employed Ratio, Return on Assets Ratio, Return on Net Worth Ratio, Earnings per Share Ratio. This study is aims to find the profitability parameter of pre and post merger of the selected FMCG companies.

1.2 REVIEWS OF LITERATURE

Rajeshkumar and Rajib (2007) conducted an empirical examination among the sample of 227 acquired and 215 target firms merged during 1993-2004. It is revealed that the size of target was much smaller compared to the acquirer firms. The acquirer firms have higher cash flow, P/E ratio, book value, liquid assets and lower debt to total assets ratio. And it is found that the less the liquidity position, the greater the possibility of the firm to become target. The larger firms are less likely to become acquisition targets.

Nedunchezhian (2013) analyzed the impact of financial performance of commercial banks in the post-merger period. The first test compared and analyzed the financial performance in the areas of capital adequacy ratio, management efficiency ratio, earning, profitability and leverage ratio. The second test determined the financial performance before and after the merger activity. Seven banks that merged during the period 2006-2010 were analysed, and the results show that there was better performance in the growth rate of assets & total deposit, current ratio and quick ratio, and the overall results confirm that there was better improvement in the post-merger period.

Honey Gupta (2016)analyzes the pre- and post-merger financial performance of State Bank of India with the help of various financial parameters such as investment ratios, management efficiency ratios, debt coverage ratios, leverage ratios, profitability ratios and profit and loss account ratios. Paired sample t-test is applied for the purpose of testing the statistical significance of various parameters. The study is based on secondary data covering eight years annual data of pre- and post-merger period. The study reveals that the State Bank of India (SBI) does not show any significant improvement in the financial performance in the post-merger period. There are some of the financial parameters that have shown significant improvement during the post-merger period while most of the parameters have not shown significant improvement during the post-merger period.

1.3 STATEMENT OF THE PROBLEM

The increased competition in the global market has also prompted the Indian companies to go for mergers and acquisitions. In India, the early mergers and acquisitions were arranged either by the government agencies or by the financial institutions within the framework of a regulated regime. A spin-off of Indian FMCG companies taking the merger route for further growth is the trend of other corporates setting up greenfield ventures abroad. Therefore, most Indian companies regard mergers and acquisitions as a path to prospective growth. The present study focuses on the role of institutional and financial developments on mergers and acquisitions related to FMCG industry with a special attention to the role played by the Indian companies. The present study is based on the following question:

- Are the sample companies profitable?

1.4 SCOPE OF THE STUDY

The study showed the benefits of mergers and acquisitions. It was possible to understand whether there was any significant improvement in the performance of selected companies. This study will become the basis for suggesting acquisition in the case of other companies.

1.5 OBJECTIVE OF THE STUDY

- To evaluate the performance of profitability of the select FMCG companies during the pre- and post-merger periods.

1.6 RESEARCH METHODOLOGY

1.6.1 DATA COLLECTION

The study is based on the secondary data taken from the annual reports of selected units and CMIE Prowess Data base.

1.6.2 SELECTION OF THE SAMPLE

Data on operating performance ratios for three years prior and three years after the acquisition for each acquiring company in the sample was extracted from Prowess database of CMIE. The final sample included 3 cases of mergers, in the defined period of study. The selected companies are

1. Colgate Palmolive Private Ltd.(Pre merger-2006-07,2007-08,2008-09: Post merger-2010-11,2011-12,2012-13)
2. Dabur India Ltd.(Pre merger-2006-07,2007-08,2008-09: Post merger-2010-11,2011-12,2012-13)
3. Hindustan Unilever Ltd. (Pre merger-2006-07,2007-08,2008-09: Post merger-2010-11,2011-12,2012-13)

1.6.3 PERIOD OF STUDY

The pre-merger and post-merger averages for a set of key financial ratios were computed for 3 years prior to, and 3 years after, the year of merger completion (or the year of approval when the time of merger completion is not available). The merger completion year was denoted as year 0.

1.6.4 TOOLS AND TECHNIQUES

The profit performance of selected companies were analysed with the help of ratios i.eNet Profit Ratio, Return on Capital Employed Ratio, Return on Assets Ratio, Return on Net Worth Ratio, Earnings per Share Ratioand Paired Sample‘t’ test was applied to test the difference in the average of selected variables before and after merger and acquisitions and the data have been analyzed with the help of SPSS and MS-Excel.

1.6.5 LIMITATIONS OF THE STUDY

The study is limited to the small sample of Indian FMCG companies, so the results of the study are only indicative and not conclusive. Moreover, accounting ratios used in the study are taken from CMIE data base.

1.7 ANALYSIS AND INTERPRETATIONS

Table 1.7.1
Analysis of Profitability Ratios

Ratio / Year	Net Profit Ratio		Return on Capital Employed Ratio	
	Pre Merger	Post Merger	Pre Merger	Post Merger
Colgate Palmolive Ltd.	18.79	4.32	49.38	4.28
Dabur India Ltd.	18.26	18.26	41.53	28.36
Hindustan Unilever Ltd.	14.73	13.57	40.81	42.09

Source: Annual Reports published by CMIE Prowess database

The table 1.7.1 shows the data regarding liquidity Ratios of selected companies duringpre and post merger period.

Net Profit Ratio

The mean value of net profit ratio during pre-merger period ranges between 14.73 and 18.79 and the mean value of post-merger period ranges between 4.32 and 18.26. It is concluded from the above table that the net profit ratioof the select FMCG companies during the post-merger period compared to the pre-merger period shows lower in the case of Colgate Palmolive Ltd. and Hindustan Unilever Ltd. This reveals that the company has adopted cost control measures effectively.

Return on Capital Employed Ratio

The mean value of return on capital employed ratio during pre-merger period ranges between 40.81 and 49.38 and the mean value of post-merger period ranges between 4.28 and 42.09. It is concluded from the above table that the return on capital employed ratioof the select FMCG companies during the post-merger period compared to the pre-merger period shows lower in the case of Colgate Palmolive Ltd. and Dabur India Ltd.and in the other case it is positive compared to the pre-merger period.This is due to the fact that these companies had utilised capital in a viable way so as to maximise their stakeholders' return.

Table 1.7.2
Analysis of Profitability Ratios

Ratio / Year	Return on Assets Ratio		Return on Net Worth Ratio		Earnings per Share Ratio	
	Pre Merger	Post Merger	Pre Merger	Post Merger	Pre Merger	Post Merger
Colgate Palmolive Ltd.	15.59	21.74	13.19	32.99	15.75	32.60
Dabur India Ltd.	17.82	22.56	3.63	2.92	3.60	3.01
Hindustan Unilever Ltd.	12.25	10.87	9.54	13.54	7.84	12.14

Source: Annual Reports published by CMIE Prowess database

The table 1.7.2 shows the data regarding liquidity Ratios of selected companies during pre and post merger period.

Return on Assets Ratio

The mean value of return on assets ratio during pre-merger period ranges between 12.25 and 17.82 and the mean value of post-merger period ranges between 10.87 and 22.56. It is concluded from the above table that the return on assets ratioof the select FMCG companies during the post-merger period compared to the pre-merger period shows better level in the case of Colgate Palmolive Ltd. and Dabur India Ltd. and in the other case it is lower compared to the pre-merger period.It is concluded that the contributing factors for the declining return on assets is due to the purchase of more assets during the post-merger periods.

Return on Net Worth Ratio

The mean value of return on net worth ratio during pre-merger period ranges between 3.63 and 13.19 and the mean value of post-merger period ranges between 2.92 and 32.99. It is concluded from the above table that the return on net worth ratioof the select FMCG companies during the post-merger period compared to the pre-merger period shows better level in the case of Colgate Palmolive Ltd. and Hindustan Unilever India Ltd. and in the other case it is lower compared to the pre-merger period.It signifies the issue of fresh equity capital and accumulation of internal accruals during the post-merger periods.

Earnings per Share Ratio

The mean value of earnings per share ratio during pre-merger period ranges between 3.60 and 15.75 and the mean value of post-merger period ranges between 3.01 and 32.60. It is concluded from the above table that the return on assets ratioof the select FMCG companies during the post-merger period compared to the pre-merger period shows better level in the case of Colgate Palmolive Ltd. and Hindustan Unilever Ltd. and in the other case it is lower compared to the pre-merger period.This indicates that the management is protecting more interest of the shareholders by paying more dividends.

Table 1.7.3
Paired Sample 't' test

Ratio / Year	Colgate Palmolive Ltd.	Dabur India Ltd.	Hindustan Unilever Ltd.
Net Profit Ratio	H_1	H_1	H_1
Return on Capital Ratio	H_1	Ho	Ho
Return on Assets Ratio	Ho	H_1	Ho
Return on Net Worth Ratio	H_1	Ho	H_1
Earnings Per Share Ratio	Ho	H_1	H_1

Source: Annual Reports published by CMIE Prowess database

The table 1.7.3 shows the performance of selected companies by using Paired Sample 't' test during pre and post merger period.

H0:There is no significant relationship between pre and post merger period.

H1:There is a significant relationship between pre and post merger period.

1.8 FINDINGS

The key findings of the study relating to analysis of profitability performance of the select FMCG companies in keeping in view the findings of this study were summarised below:

- The **net profit ratios** of Dabur India Ltd. earned the net profit during the post-merger periods. This reveals that the companies have adopted cost control measures effectively.
- The **return on capital employed ratios** of Hindustan Unilever Ltd. was better in return on capital employed during the post-merger periods. This is due to the fact that these companies had utilised capital in a viable way so as to maximise their stakeholders' return.
- The **return on assets ratios** of Colgate Palmolive Ltd. and Dabur India Ltd.
  were found to be satisfactory and other units were not satisfactory. It is concluded that the contributing factors for the declining return on assets is due to the purchase of more assets during the post-merger periods.
- The **return on net worth ratios** of Colgate Palmolive Ltd. and Hindustan Unilever Ltd. were satisfactory. It signifies the issue of fresh equity capital and accumulation of internal accruals during the post-merger periods.
- The **earnings per share ratios** of Colgate Palmolive Ltd. and Hindustan Unilever Ltd. were found to give a positive signal and other units were found to give a negative signal. This indicates that the management is protecting more interest of the shareholders by paying more dividends.

1.9 CONCLUSION

Better utilization of firm's resources leads to value creation. In this study, we empirically investigated the effect of profitability using a sample of Indian FMCG companies. Accordingly, the findings of the results indicate that both pre and post-merger periods are positively associated with firm's profitability. Based on the findings of the study, it conclude that these results can be further strengthened if the firms manage their income sources in more efficient ways which will ultimately increase firm's profitability.

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