JETIR.ORG ISSN: 2349-5162 | ESTD Year : 2014 | Monthly Issue
JOURNAL OF EMERGING TECHNOLOGIES AND INNOVATIVE RESEARCH (JETIR)
An International Scholarly Open Access, Peer-reviewed, Refereed Journal

A Study on Mergers and Acquisitions in Telecom Industry with Reference to Vodafone and Idea

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INTRODUCTION

Abstract: Mergers and acquisitions are the only way to gain competitive advantage at home and abroad. Today, the telecom sector has grown immensely by 65%. India is the second largest telecommunications market in the world. This project aims to understand the merger and acquisition of Vodafone and Idea. In this project, we considered the impact on the financial position of Vodafone and Idea. The financial statements of both companies before and after the merger helped us in deriving interpretations and findings.

Keywords: Mergers, Acquisitions, Financial, Company, Vodafone, Idea.

Merger & Acquisition

Mergers and acquisitions occur when ownership, assets, and liabilities of one company are transferred to another company to expand business, reduce competition, expand workforce, infrastructure, and so on. It is essentially corporate strategy, corporate finance, and management trading involving the buying, selling, and merging of various companies that can support, finance, or help companies grow in a particular industry to grow rapidly. Such actions are usually voluntary and involve an exchange of shares or a cash payment to the target. Share swaps are often used as an option because they share the risks associated with M&A among the shareholders.

Objective of Merger and Acquisition

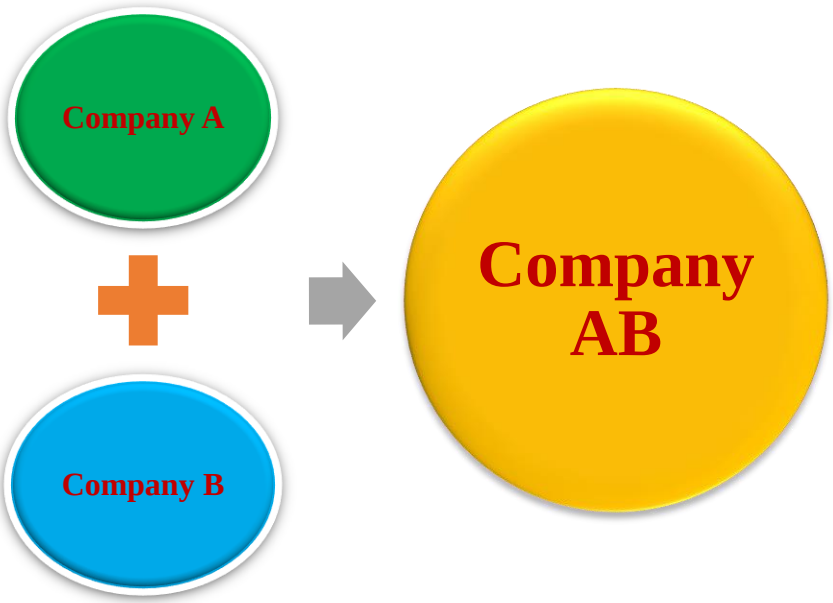
1. **Security:** There is a security against failure enjoyed by smaller companies when they merge with a huge industry giant. The larger firm has the capacity and financial resources to handle expensive lawsuits and paddle through the market storms. On the other hand, when faced with similar situations, small businesses tend to go bankrupt on their own.
2. **Scales of Economies:** The main objective of M&As is basically to achieve economies of scale, that is, to increase the final output and the firm size as a whole. The cost per item is reduced by spreading the fixed cost over a huge quantity. The efficiency is also increased by specialization of the production process leading to cost advantages.
3. **Incentives to Managers:** M&As are basically inspired by the goals and personal interests of the company's top management. It is usually guaranteed that the managers enjoy more prestige and power after an M&A. This is also referred to as 'empire building' where the managers begin to favour the size of the firm more than the actual performance.
4. **Diversification**: Many times, M&As take place for the purpose of diversification such as offering new products and services or entering into new markets. Furthermore, the risks are also diversified relating to the operations of a company. The shareholders are not always happy with the situation where an M&A occurs with the aim of risk diversification.
5. **Tax Benefits**: When two or more firms merge or during an acquisition, many tax implications arise. Due to an M&A, many tax benefits can be enjoyed by using net operating losses to shield income or taking advantage of existing tax laws.
6. **Eliminating Competition**: The M&As are done on a large scale for the purpose of eliminating competition in the industry. It is usually done for substantially decreasing competition or for the creation of a monopoly status in the market. This eliminated competition and a solo status can prove very beneficial to the company. They can have the freedom to keep their prices higher and enjoy profits for the business.

Meaning of Merger

Fusion is the merger of two existing companies into a new company. The main reason one company merges with another is for growth or expansion. It is carried out voluntarily by companies and a new legal entity is created. The term merger simply reflects the merger of two companies by mutual consent. This usually involves some form of stock allocation, in which the initiating company offers shares in exchange for the shares of the merging companies, creating a single entity.

Example of Merger

let us assume there are two companies, Company A and Company B both the companies come together for the reason of expansion or growth then a new legal entity named Company AB is formed.



(Source: Drawn by Authors)

Meaning of Acquisition

Acquisition is when one company takes over or purchases other company. This means everything from its assets, liabilities, and brand image, all become one entity. As a result, it is often seen to produce financial benefits as the combined company becomes more efficient.

Companies acquire other companies for various reasons. They may seek economies of scale, diversification, greater market share, increased synergy, cost reductions, or new niche offerings.

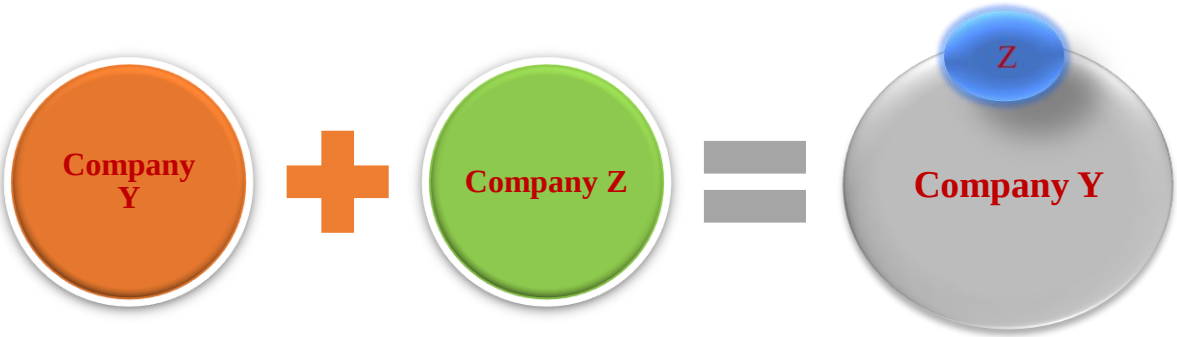
Parties involved in Acquisition:

Acquirer: The person who purchases the company is called acquirer.

Acquiree: The company that has been subject to purchase is called acquiree.

Example of Acquisition

Let us assume there are two companies, company Y which is operating in a large scale and there is a company Z which is working in a comparatively smaller scale, Company Y can purchase the company Z and make it one entity namely company Y



(Source: Drawn by authors)

Types of Mergers and Acquisitions

Horizontal Merger

- It is a merger or acquisition of companies in same industry or offering same product or service
- Example:merge r of any two cosmetics companies

Vertical Merger

- It is a merger or acquisiton when two companies operate at different stages of supply chain
- Example:merge r of a laptop production company with its parts supplier

Conglomerate Merger

- It is a merger or acquisition when two companies from completely different industries join together
- Example:merge r of a soft drink producing company with watch making company

Concentric Merger

- concentric merger is when two companies operate in the same industry,have same customer but offer different products
- Example: merger of a commercial bank with NBFC'S

Differences Between Merger and Acquisitions

Basis	**Merger**	**Acquisition**
Meaning	Merger is collaboration of two companies to form a new company	Acquisition is when a company is purchased by another company where the assets, liabilities, goodwill becomes one entity.
Company size	The companies which merger are of the same size	The size of the acquirer is more than the size of acquiree
Power	Both the companies have equal say	Acquirer has the greater power
Title	A new entity is formed	There is no need to form a new entity
Decision	Voluntary or mutual	Can be voluntary or hostile
Purpose	Decrease competition	Growth and expansion
Example	Company A+ Company B=Company AB	Company X purchases company Y, hence company Y becoming a part of company X

(Source: Drawn by author)

Review of Literature

K. Naveen Kumar (2022), he examined the study intended to identify the arrangements of the Merger and Acquisition in the telecom industry by analysing the previously available literature.

Karan Singh (2021), The Vodafone India and Idea Merger meant an increase in competition, which means that clients will be paying low prices. Merger increased their reach and it now jointly offers 4G services to a broader range of customers.

Bushra Tungekar (2021), Both the companies had said in their statement that the synergy would be extremely cost-effective. The estimated savings annually would go up to 14,000 crores. The savings would be in the form of both capital expenditure as well as operating cost.

Aditya Kasiraman (2020): To deal with attacks from Jio, the operators went to integration mode, discovering the spectrum, minors, infrastructures etc.

Vijay Joshi (2019), He examined the study in which Vodafone and Idea announced their merger in 2017, which had a major impact on the Indian telecom sector. This was a major consequence of Jios Cruising's dominance of the industry, which prompted other big players to take precarious moves to assert their position in the Indian telecoms market. Vodafone India was the second largest player in the Indian telecoms industry in terms of subscriber base, while Idea Cellular Limited has the third largest subscriber base in India. Idea Cellular was a subsidiary of Aditya Birla Group. Not only did this merger create a telecoms giant, but it had far-reaching implications for the industry, services, employees and consumers, and has fueled further mergers in the telecoms sector.

Ashok Panigrahi (2019), He examined that the main reason for the Vodafone-Idea merger was to combat Reliance Jio's increasing dominance in the Indian sector. This will lead to a brutal price war between the big players in this industry. This merger has led to further mergers and acquisitions of other telecommunications companies. The assets of Telenor India and Reliance Communication were contributed by Bharti Airtel. These effects were also observed on the savings synergies and the spectrum in rapid growth.

Wiboon Kittilaksawong, Sindhuja Kandaswamy (2018): The Indian Telecom market was witnessing a fierce price war, especially from an aggressive entry of a new player Reliance Jio info (Jio) with a predatory pricing strategy.

Reuters staff (2018): Himanshu Kapania has stepped down as managing director of Idea Cellular, but will continue as a non- executive director on the merged entity's board, the merged entity would be a formidable rival to billionaire Mukesh Ambani's Reliance Jio Infocom.

Press Trust of India (2017): The deal gives Vodafone India an implied enterprise value of Rs. 82,800 crores and Idea Rs. 72,200 crores. Upon completion of the transaction, the UK company will own a 45.1 per cent stake in the combined entity, while Aditya Birla Group, Ideas' parent company, after paying Rs. 3,847 crore in cash for a 4.9 per cent stake. The remaining 28.9 percent are held by other shareholders. Stock of Idea traded at Rs. 79.45, up 6.64 percent from its previous close in the afternoon session.

Gadgets360 staff (2017): Vodafone and Idea complement in many ways, like in terms of – geographical coverage, spectrum holdings and rural/ urban subscriber mix (with a few exceptions in some circles). Now that this is announced the key benefits the combined entity needs to exploit are synergies across operational costs.

Dev Chatterjee (2017), he examined intense competition from cash-rich Reliance Jio, The Aditya Birla group and British telecom giant Vodafone Plc on Monday announced the merger of their Indian wireless telephony businesses, creating the largest telecom operator in the country.

Objectives of the Study

1. To understand the meaning of Mergers and Acquisition.
2. To study the financial performance of the companies before and after the Merger and Acquisition.

Research Methodology

Data Collection

Secondary Data: The data collected from readily available sources which helps in further processing of information is called secondary data.

The data for the research is based on secondary data. The financial statements were taken from the published data i.e., company's official websites, money control and zee business.

Scope

The scope of the research is based on data of three years pre-merger (2015-16, 2016-17, 2017-18) and three year's post-merger (2019-20, 2020-21, 2021-22) and the base year is 2018-19.

Accounting Tools

The study was conducted using Ratio Analysis

Ratios

The following ratios were used for the analysis of the financial statements:

1. Asset Turnover Ratio
2. Current Ratio
3. Debt-Equity Ratio
4. Inventory Turnover Ratio
5. Net Profit Ratio
6. Return on Capital Employed
7. Return on Equity

Asset Turnover Ratio

Asset Turnover Ratio is a type of Efficiency Ratio. This ratio helps us to compute the value the company's Revenues with respect to the value of its assets. This ratio indicates that if the asset turnover ratio is high the more efficient it is at generating revenue from its assets. Therefore, if the asset turnover ratio is low it indicates that it's not efficient enough.

Asset Turnover Ratio = Net Sales / Average total assets

Current Ratio

Current Ratio is a type of a Liquidity ratio. This Ratio shows the company's capacity to repay all short-term obligations and loans which are due within one year. It helps investors in understanding how company can maximize its current assets. The ideal current ratio is 2:1.

Current Ratio = Current Assets / Current liabilities

Debt-Equity Ratio

Debt- Equity Ratio is a specific type of a Solvency Ratio. This ratio can be used to assess the long -term financial stability of a business. This ratio shows the relationship between the company's total debt and total equity.

Debt Equity Ratio = Debt / Equity (Or)Outsiders fund / Shareholder's funds

Inventory Turnover Ratio

Inventory Turnover Ratio is a type of an activity/performance/turnover ratio. It shows the number of times a company has sold and replaced its Inventory during a given period of time. The calculation of Inventory turnover ratio can help various businesses to make better decisions regarding marketing and pricing of new inventory.

Inventory Turnover Ratio = Cost of Goods Sold / Average Inventory

Net Profit Ratio

Net profit ratio is a type of profitability ratio. Net profit ratio is nothing but it is the ratio of after-tax profits to net- sales. Its shows us the remaining profit after all costs of production, administration, and financing have been deducted from sales, and income taxes recognized. Higher the net profit ratio better it is.

Net profit ratio = Net profit *100/ Sales

Return on Capital Employed

Return on capital employed is a type of a profitability ratio, it is used to know a company's profitability and capital efficiency. With the help of this ratio, we can easily get to know how much profit is earned by a company and how well a company is using its capital in profit generating.

Return on capital employed = Earnings before interest, dividend and tax*100/ Capital employed

Return on Equity

Return on Equity (ROE) is a financial ratio which tells us how much net income a company is generating if per dollar is investing in it. This percentage is the most important tool for the investors to know how efficiently a company uses its capital to generate profit. Return on Equity can also be measured on 'Assets-Liabilities'.

Return on Equity= Net Income / Shareholders' funds

Data Analysis and Interpretation

Ratios Table

Particulars	**Idea**	**Vodafone**	**Vi**
	Pre (Mean)		**Post (Mean)**
Asset Turnover Ratio	0.91	0.729	20.09
Current ratio	0.87	2.261	0.22
Debt – Equity	4.633	1.486	2.97
Inventory Turnover Ratio	1157.526	134.386	34883.06

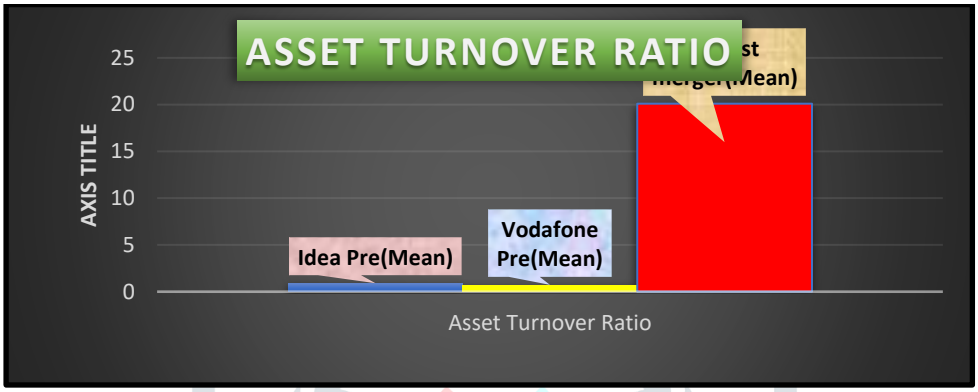
Net Profit Ratio	-13.33	-11.256	-114.806
Return on Capital Employed	5.69	4.253	-5.576
Return on Equity	-16.06	-4.89177	-411.813

(Source : Data was collected from moneycontrol.com and compiled)

Interpretation

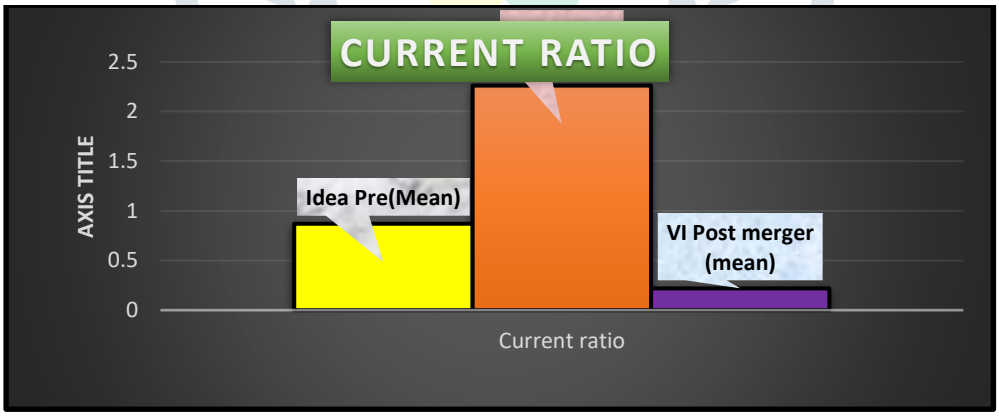
Asset Turnover Ratio

From the table we can observe that the asset turnover ratio of Idea, Vodafone is 0.91,0.729 respectively. Both the companies are not efficient in generating revenue from assets. After the merger we see a good increase in the asset turnover ratio so we can comprehend that need of the merger is satisfied.



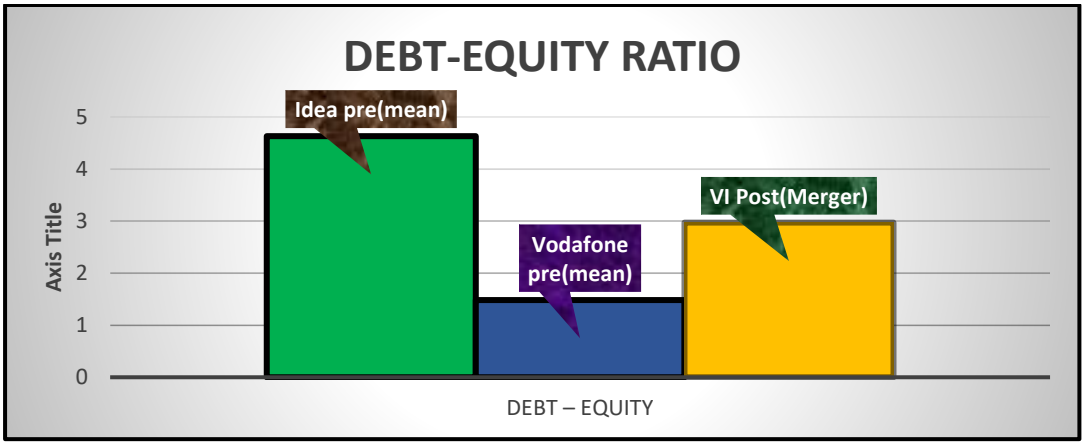
Current Ratio

The ideal ratio of current ratio is 2:1. The current ratio of Idea, Vodafone are 0.87 and 2.261 respectively. From this we can understand that the liquidity position of Idea was not good compared to Vodafone. But post- merger we can see a fall in the liquidity position of the company to 0.22. The company must work on improving its liquidity position.



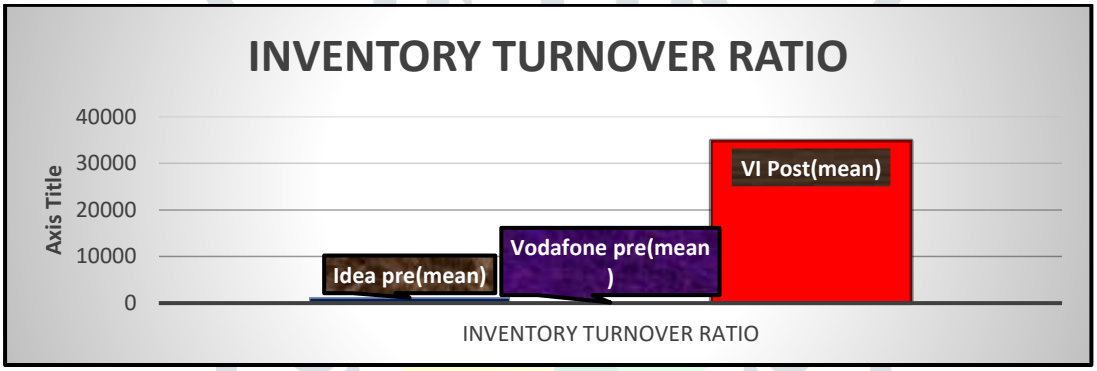
Debt-Equity Ratio

The debt-equity ratio of around 2 or 2.5 is generally considered good. The Debt-Equity ratio of Idea and Vodafone are 4.633 and 1.486. Since the debt-equity ratio of Idea company is more the interference of the lenders will be more. In case of Vodafone company, the debt-equity ratio is more than the ideal ratio which indicates the owners can have higher level of control in the business with limited capital. Post-merger the debt-equity ratio is at par with the ideal ratio.



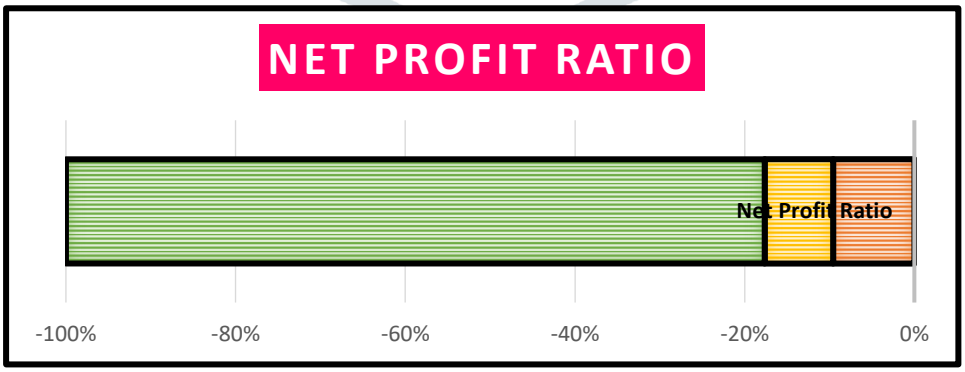
Inventory Turnover Ratio

The inventory turnover ratio of Idea company is too high which states there is an overstocking. The inventory turnover ratio of Vodafone is lesser compared to idea. The high inventory turnover ratio of idea indicates good sales but it is also not considered to be a good sign because it affects the long- term funding requirements of the company. The post-merger ratio is also high so the company must take few precautionary steps like reducing purchase quantity, better forecast etc.



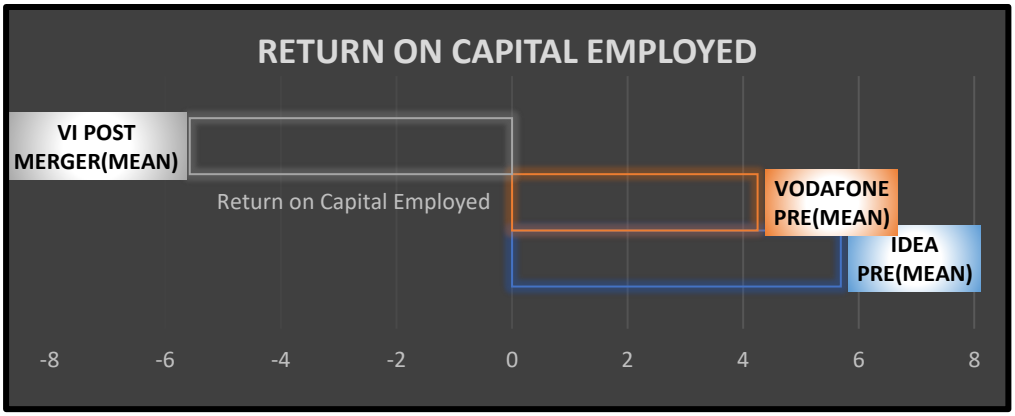
Net Profit Ratio

The net profit ratio of Idea (13.33) and Vodafone (11.256) indicates that the companies are unable to cover the expenses of the business from the revenues earned by them. The situation post-merger has also not improved hence the companies needs to focus on their performance.



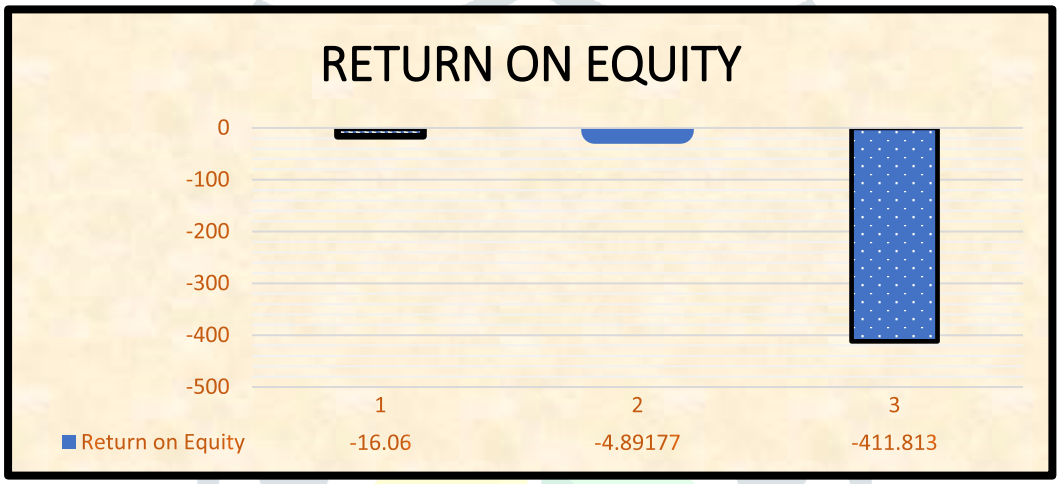
Return on Capital Employed

The return on capital employed measures the ability of the company to earn for every rupee invested in the company. The Return on capital employed of Idea is better compared to Vodafone. The post-merger return on capital employed is (5.5) which indicates a net operating loss.



Return on Equity

Both the companies are having a negative return on equity which means that there are some restructuring processes going on hence there might be some improvement in the return on equity ratio. But if the same continues then there is a need to worry about the performance of the company.



Findings

From this study we found out that-

1. The major reason for merger of Vodafone and Idea was the dominance of Jio in the telecom industry.
2. The merger of Vodafone and Idea is the second largest merger after the Bharti Airtel, in the telecom industry, hence this merger is expected to hold a strong position in the telecom market.
3. Post-merger, the Vodafone group owns approximately 45% stake in the merged entity whereas Idea Ltd. Has a share of approximately 26%.
4. The merger gave a higher stake to the promoters of Idea as compared to Vodafone India so that in the long run both the companies are able to gain access to equal hold.
5. We have understood the various ratios, their significance and interpretation of these ratios
6. Analysis of financial position and performance of the company's pre-merger and post-merger
7. Through this merger, Both Vodafone India and Idea cellular will overcome their debts and a large sum of credit will be infused in the system.
8. This merger between Vodafone and Idea has saved both these telecom companies from selling their businesses.

Conclusion:

Many companies find that the best way to get ahead is to expand ownership boundaries through merges and acquisitions. Separating the public ownership of a business segment offers more advantage. Merges and acquisitions have more advantages rather than disadvantages, it creates synergies and economies of scale, expanding operations and cutting costs.

With the help of merger and acquisitions, investors have an idea that a merger will deliver enhanced market power and if we invest, we will get good returns.

In the month of September 2022 Vodafone and Idea rebranded itself. The company used the initials "Vi" to rename itself, thus rebranding took place after 2 years after the merger happened, this shows the spirit of integration.

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