CHAPTER 1 INTRODUCTION

The Malaysian and world business scene is becoming ever more competitive as the effects of globalisation take shape. For individual firms, the economic role of mergers and acquisitions (M&A) is to assist in achieving or maintaining their competitive advantage by anticipating and adjusting to change. Powerful long-term change forces have been driving M&A activity in recent decades. Technological change impacts every industry. The internationalisation of markets and the globalisation of competition have encouraged M&A activities. The role of M&A is to assist firms and economies in adjusting to opportunities and change. In 2000, worldwide M&A activity was valued at US$3.6 trillion. (Source: Mergers and Acquisitions Magazine)

M&A activities have increased as part of a worldwide increase in corporate restructuring. Many firms, both large and small, have undergone M&A exercises in order to remain competitive against the onslaught of global conglomerates and Malaysia is no exception. With the formation of the World Trade Organisation (WTO), member countries would have to liberalise trade and reduce barriers in stages. The globalisation of trade means that mergers are inevitable part of preparations to face looming competition from foreign players. Indigenous firms especially in developing countries have become even more vulnerable to competition from the foreign giants and thus size became an imp consideration around the turn of the millennium.

The most apparent case in Malaysia is the consolidation of the financial institutions whereby the local banks and finance companies have merged together and all but ten anchor banks remain. The big banks in developed countries have merged into mega financial houses and in order to compete against them, the local banks are expected to undergo further consolidation in the near future.

1.1 Definitions and terminology

Mergers and acquisitions (M&A) include mergers, acquisitions, divestitures, alliances, joint ventures, restructuring, minority investments, licensing, and franchising as well as international activities. M&A terminology can vary considerably depending on the text used. The definitions used in this study follow that of Fauzias (2003).

An *acquisition* is any transaction in which the buyer acquires all or part of the assets and business of a seller, or all or part of the stocks or other securities of a seller. There are two main types of acquisitions; asset and stock acquisitions. An *asset acquisition* is a transaction in which the buyer acquires all or part of the assets and business of the seller. A *stock acquisition* is a transaction in which all or part of the outstanding stocks of the seller is acquired from the stockholders of the seller.

A *merger* is a combination of two companies where one loses its corporate existence and the surviving company acquires both the assets and the liabilities of the merged entity

A *consolidation* is a combination of two companies whereby an entirely new company is formed. Both the old companies cease to exist and their existing shares are exchanged for shares in the new company.

A *take-over* is a transaction where the buyer acquires control over the assets of the target company, either directly or indirectly through the control of either voting rights or the management of the target company.

A take-over can also occur either through tender offer or proxy contests. In a tender offer, acquirers make a direct offer to shareholders to buy some or all the shares of the target firm. Insurgent groups attempt to gain controlling seats on the board of directors via proxy contests.

This study focuses primarily on stock acquisitions. These acquisitions are essentially take-overs since the criterion involves the acquirer obtaining at least 51% of outstanding shares.

1.2 M&A history in Malaysia

Mergers and acquisitions (M&A) in Malaysia started in the 1970's in the plantations sector with significant foreign involvement. In the 1980's, growth was rapid especially in the industrial sector and coupled with the privatisation policy, many companies diversified their businesses. Malaysian companies then started involving in acquisitions both local and abroad in the 1990's. The late 1990's were the time for mergers of banks and financial institutions. That reduced the numbers from 54 financial institutions to 10 anchor banks.

The onset of the Asian financial crises caused many companies to be in financial distress especially the highly leveraged ones. It was argued that over-diversification though M&A was a key reason for it. The Asian financial crises affected countries like Thailand, Indonesia and South Korea even more. The economic reforms as a result of the crises also resulted in foreign take-over on their conglomerates.

1.3 Objectives of study

This paper aims to analyse the short-term price effects of mergers and acquisitions (M&A) involving Malaysian firms listed on the Bursa Malaysia, formerly known as the Kuala Lumpur Stock Exchange (KLSE). This issue focuses on the extent to which recent corporate acquisitions announced in Malaysia after the Asian Financial Crises resulted in generation of shareholder value.

Numerous studies in finance and strategy have shown that acquisitions are a mixed blessing for shareholders of acquirer firms, even when they create synergies. In fact, the benefits are usually enjoyed by the target firm's shareholders with a return of over 30 percent on average (Jensen and Ruback 1983; Bradley, Desai, and Kim 1988) although recent studies exhibit diminishing returns. In most cases, acquirer shareholders about break-even while some mergers lead to significant losses for the acquirers.

Short-term cumulative abnormal returns will reflect changes in the expected future cash-flows to shareholders resulting from future synergies in the merged entity or from wealth redistribution among shareholders.

Value creation for the shareholders of the target and acquirer firms is only a partial measure of the net social value generated by a corporate restructuring decision. Net social value includes changes to other economic agents such as increases or decreases in consumer welfare. Many acquisitions also involve corporate restructuring leading to lay-offs and other significant changes with direct implications for the welfare of other stakeholders such as workers, suppliers or communities in which the firms operate.

1.4 Significance of study

Recent studies on mergers and acquisitions (M&A) tend to focus on the financial industry but this study aims to provide a holistic view on M&A activities after the Asian financial crises and its benefits to shareholders. The focus on shareholder return brings the advantage of being easy to observe. More decisively, they also represent the best estimate at the time of the transaction of the expected present discounted value to shareholders generated by the transaction. The findings and results here should be of interest to academicians, business analysts and corporate strategists as well as existing shareholder and investors.

1.5 Organisation of study

The paper is organized as follows. The next section reviews the literature of the broad evidence on the impact of mergers and acquisitions (M&A) on shareholder value creation. Section 3 describes the research hypotheses, methodology, data used for this analysis and discusses the way in which the data was obtained and collated. Section 4 presents the statistics, descriptive information on cumulative abnormal returns from merger announcements as well as various results and analysis. Section 5 provides a summary of the findings, conclusion and provides recommendations for future research.