

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Indonesia was able to realize satisfying economic performance lately. It is proven by five percent of economic growth in the fourth quarter of 2015, which was surpassing previous quarter accomplishment. Even though Rupiah was depreciated by 9.5 percent, it was still superior compared to Brazil (31%), Malaysia (28%), and Turkey (20%) (www.katadata.co.id, retrieved on 16th October 2016).

Some analysts contended that this condition arose due to internal and external factors. Internally, According to Asia Development Bank, government efforts to boost infrastructure projects became the core stimulus of national economic improvement. Externally, increase of labor wage in other developing country such as China makes their country less attractive to be invested in, which moreover will inflict investors to shift their investment to Indonesia (www.liputan6.com, retrieved on 3rd March 2017).

Rapid growth of Indonesian economy leads to tighter and more complex competition among existing companies. This situation emboldens some companies to take strategic decisions with the aim of maintaining their sustainability and improving their performance. Strategic decision can be categorized into investment decision, dividend decision, and costing decision. One of the investment decisions that can be used by company is in the form of expansion which facilitates company to expand and cultivate its business. The expansion itself can be categorized into two types which are internal and external. An example of the external expansion strategy is by incorporating several businesses (Kuncoro, 2014). Types of incorporation which are commonly practiced in last two decades are merger and acquisition (M&A).

Merger defined as the combination of two or more companies into one using the existed legal status of one of the companies, whereas the status of others is abolished. In the other hand, based on UU No. 40 Tahun 2007 tentang Perseroan Terbatas (“UUPT”), acquisition constitutes the takeover of some or whole shares of other company so that the acquiring company possesses the control rights of target companies. Both definitions’ are distinct but principally own same meaning in terms of business combination so that both methods are interchangeable.

Moin (2003) stated that M&A can be approached from two perspectives which are corporate finance and strategic management. In the perspective of finance, merger and acquisition is one of the long haul investment decisions that need to be analyzed and investigated from the business feasibility aspect. Meanwhile from the perspective of strategic management, merger and acquisition are alternative growth strategy through external way to accomplish companies' goals.

For many years, M&A has become one of the most favorite strategies in the business world. It was starting to boom among multinational companies in United States since 1895s with a great merger movement as a marker (Lamoreux, 1985). The 80s era is considered as golden age for merger and acquisition for US. It is recorded that 55,000 acquisitions have been happened, making this age named as 'merger mania decade' (Hitt, 2012).

In Indonesia, the history began in 1950s along with nationalization policy even though those were not considered as a pure M&A M&A started to be a hot issue for Indonesian economic observer, scientist, and practitioner in 1990. Thirty two M&A cases which involved 79 companies have happened in the period of 1989-1992 (Kuncoro,2014)

However, the latest data from KPPU (Komisi Pengawas Persaingan Usaha) demonstrates that the trend of M&A activities in Indonesia is decreasing. According to Bruce Delteil, APAC Lead of Accenture Strategy M&A, the

weakening of M&A trend was started when the Indonesian government started issuing policy that is considered contradictive with investment climate such as limitation of foreign ownership, and establishment of investment negative list. In addition, instability of political atmosphere led to cancellation of some M&A process in 2015 (www.kontan.co.id, retrieved on 1st December 2016).

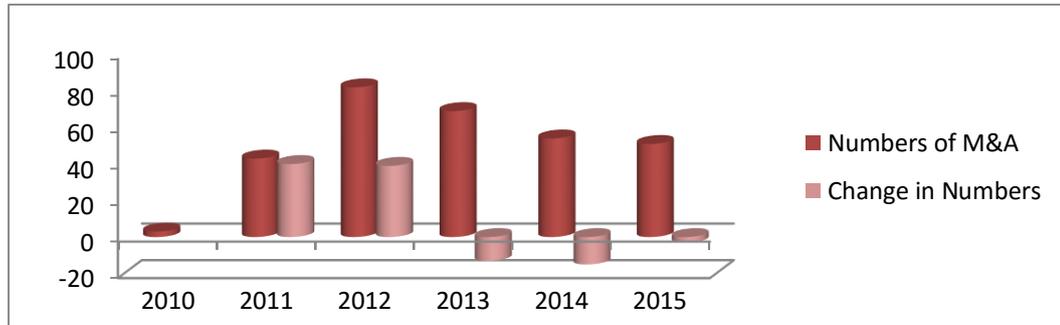


Figure 1
Volume of Mergers and Acquisitions deals announced in Indonesia in 2010-2015
Note. www.sahamok.com (Retrieved on 10th October 2016)

Furthermore, Merger and acquisition are often seen as controversial decision since it may cause dramatically and complex effects. One of the negative influences can be seen from employees' perspective since this discretion is often followed by fantastic number of employee layoff. In the case of Bank Mandiri, more than 11,000 employees are forced to retire earlier whereas in Bank Permata, the dismissal involves 2,350 workers. Other controversies and intrigues in various forms are also arising as a consequence of M&A. For instance this media is utilized to magnify asset amount, evict acquired company management, or even enlarge compensation for its own executive (Nugroho, 2010).

Even though, there are many challenges, there are also many reasons why company likes to perform M&A. First, Merger can be implemented to evade a company from bankruptcy risk when conditions of one or both companies, which are going to be combined, are under the threat of bankruptcy. The causes are mostly because of miss management, losing market-share and inability to keep up with technology advancement. Through M&A, both companies can synergize to establish new strategy so that the risk of bankruptcy can be minimized (Motis, 2007).

Acquisition is also done with the purpose of utilizing tax incentive which is rendered due to new policy in taxation field issued by the government (Auerbach, 1987). For instance, a new product is subjected to extremely low tax values by law of taxation. The companies that produce those products are likely to become the target of M&A by the large companies on the behalf of sheltering their own income.

Another motive of acquisition is diversification. Basically, diversification is intended to reduce risk. If two or more companies in one business field perform an M&A, the company which is the outcome of M&A will own more assorted products. The diversification mechanism implies dividing risks of the company to various types of product so that the risks minimized and higher expected yield can be achieved (Markowitz, 1952).

Last but not least, M&A are directed to increase the capability of company to increase debt capacity. Amount of money a financial institution willing to lend to a company generally is based on its asset (www.city.ac.uk, retrieved on 5th October 2016). The larger the asset of a company, the bigger amount of loan that potentially realized and vice versa. Thus, the company that has performed M&A can expand the business through increase in the value of bank loans.

Those benefits irrefutably are potent factors which push a lot of companies to perform M&A strategy. One of the hottest M&A activities in Indonesian history is acquisition of Indosiar Karya Media Tbk. (IDKM) by PT Elang Mahkota Teknologi Tbk. (EMTK) in 2013. Neraca.co.id (retrieved on 1st October, 2016) stated that this agreement is executed with the purpose of synergizing Indosiar and SCTV. Furthermore, they wanted to escalate efficiency by sharing the infrastructure and production facilities yet ease capital market investors who desire to invest in television media firm (kppu.go.id retrieved on 17th June 2017).

In order to minimize any risk, before performing M&A, performance of the company that will be acquired need to be taken into account since it will determine the feasibility of a company that will be purchased. How well a company performs can be measured from the financial ratio comprising profitability, activity, liquidity, solvency, and market ratio. Moin (2003) in Nugroho (2010) stated that return on assets and return on equity can be used in profitability ratio; debt ratio and debt to equity ratio in solvency ratio; current ratio in liquidity ratio; total asset turn over in activity ratio; yet earning per share in market ratio.

However, M &A never guarantees enhancement of a company's performance. Numbers of observations have been done to test the impact of M&A towards company's financial performance and the result barely comes out in a consistent way. Kruse, Park, and Suzuki (2002) were testing long-term operating performance following all mergers between manufacturing firms listed on the Tokyo Stock Exchange (TSE) in the period from 1969 to 1992. Using a unique data set that includes the pre-merger performance of target firms, they find that the long-term operating performance following the mergers is positive but insignificant.

Sonia Sharma (2013) in her research article "Measuring post merger performance: A study of Metal Industry" attempts to study the impact of merger on the financial performance of merging companies by examining some pre-merger and post- merger financial ratios. The findings showed a marginal but not significant improvement in case of liquidity and leverage.

Beside those findings, research that need to be considered are the paper done by Mantravadi and Reddy. Mantravandi and Reddy (2008), finds out that the financial ratios of firms that acquiring cross border firm has been impacted negatively after the merger. The performances were proved to be decreased over years with the financial ratios of pre until post two years of merger as the object of

observation. Another research done in Europe by Gugler, Mueller, Yurtoglu and Zulehner (2003) show a significant decline in post-acquisition sales of the combined firm, but an insignificant increase in post-acquisition profit.

Based on the phenomenon and observation that have been discussed on research background, writer is interested in conducting a research entitled: **“Comparative Analysis on Public Companies’ Financial Performance Before and After Acquisition (Towards Acquiring Company that Registered in Indonesian Stock Exchange in the Period of 2010-2012)”** to measure the successfulness of Indonesian companies from miscellaneous industries which has already performed acquisition.

1.2 Research Problems

Based on the description of the background issues that have been raised, the formulation of the problem areas are as follow:

1. Is there any significant different on liquidity ratio of acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012 after they performed acquisition?
2. Is there any significant different on solvency ratio of acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012 after they performed acquisition?
3. Is there any significant different on profitability ratio of acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012 after they performed acquisition?
4. Is there any significant different on activity ratio of acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012 after they performed acquisition?
5. Is there any significant different on activity ratio of acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012 after they performed acquisition?

1.3 Research Objectives

Based on the stated research problem, the main objectives of the study are as follows:

1. Test the difference of liquidity ratio of the acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012
2. Test the difference of solvency ratio of the acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012
3. Test the difference of profitability ratio of the acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012
4. Test the difference of activity ratio of the acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012
5. Test the difference of market value ratio of the acquiring companies that are registered in BEI which performed acquisition in the period of 2010-2012

1.4 Research Contributions

1.4.1 Theoretical Advantages

This study made its contribution as a reference in Financial Management, by identifying the significance of acquisition towards firm's performance. This study is also expected to become a reference for further observations similar to this field of study.

1.4.2 Empirical Advantages

1. For researcher

This research is beneficial for researcher to enrich the insight about financial management and implement the theory that has been obtained during the lectures especially those that are related to impact of acquisition towards firm's financial performance

2. For investors

This research can be utilized as an input to understand the consequences of acquisition towards performance of acquiring companies so that investors will be able to decide whether to perform acquisition or not. Investors can

also replicate and apply the methodology of the research on other companies in the future to sharpen the quality their buying decision.

1.5 Research limitations

This study was conducted in order to discover the impact of acquisition towards Indonesian company's performance. This research used liquidity, solvency, profitability, activity, and market value ratio. The research only analyzes the impact of acquisition towards Indonesian company which is registered in Bursa Efek Indonesia (BEI). The research data gathering are conducted in the period of 2010-2012.

1.6 Research Outlines

Research outline explains the systematic writing of this study. The outline is divided into three chapters as follows:

Chapter I

This chapter sets up the research problem for the reader. It also provides the background information defining the issue and important terms. It specific the research objectives explored in greater detail to contribute to understand the research problems.

Chapter II

This chapter summarizes the major studies and finding that have been published on the research topic and how this study contributes or adds to what has already been studied. This chapter also states a clear description of theories that apply to research problem, an explanation of why it is relevant, and how the modeling effort addresses the hypothesis to be tested.

Chapter III

This chapter explains the detailed technical and specific activities which include the research design, sampling plan instrumentation, social tools and treatment of data.

Chapter IV

This chapter is considered as the main part of the study. It provides result of data process and discussion regarding the data.

Chapter V

Recommendation and suggestion for stakeholders and future research will be elaborated in this chapter. Summary and conclusion will also be presented.