CHAPTER I

INTRODUCTION

1.1 Background of the Study

In this globalization era, many companies have already started to expand their business by utilizing technology to maintain their existence in competitive market. The company must be able to develop more innovation as an assertion for changes. With technologies advanced, all things should be easier to approach and to connect especially in economics. International trade will be more open in this era, and will cause the business competition widely. In order to survive, one company must have the right strategies to increase the business growth performance. One of the strategies is through business expansion. The company can strengthen its presence in the market, develop and compete in carrying out business goals.

There are many reasons for enterprise expansion not only to survive in the competitive market but also to increase prestige associated with company size, new earnings potential, economics of scale, larger market shares, and management rewards. (Tamosiuniene & Duksaite, 2009)

Business growth expansion can be classified into two categories which are internal expansion and external expansion. Internal expansion is when a business start to expand its own operation without any contribution for external parties, or in other words, the expansion is through its own resources and capabilities.

For examples, maximize market and production through its scale of operations, financial and non-financial resources by assessing a company’s core competencies. Meanwhile, external expansion is a strategy to increase the asset worth and business reach by external parties through merger, consolidation and acquisition strategies even include joint ventures and franchising business model.

The larger number of business partner, the greater the net worth of the company, this signifies the stability of the company in the competitive market. When a company does not use these two strategies both internal and external, the company will not survive from rigors of business competition.

According to Durmaz (2015) Mergers and acquisition are strategic decisions in corporate world that maximize company's growth by enhancing its production and marketing operations. Mergers and acquisitions are taking place in wide areas such as information technology, telecommunication and business process outsourcing as well as in traditional businesses in order to expand the customer base, reduce competition or enter into new markets or product segments. In other words, by doing company mergers and acquisitions can save time in accessing markets and new products, because with mergers and acquisitions the profits obtained by the company will be greater because there is not only one company in it.

By merging the several businesses are considered as discourse to achieve business goal and interest that provides rapidly growth which is more attractive than normal business development. Merger of companies or takeovers of other companies is done with one the main reason is to get synergy. Synergy means that the combined value of the two companies is greater than the sum of each company value combined. In other words, mutually beneficial conditions occur when the acquisition activities get a synergy. (Dyer, Kale, & Singh, 2004) So in long-term every company aims to get more benefit after decided to acquire other company, not the opposite. The decision of a company to conduct mergers and acquisitions is an effort to improve the company's financial performance without having to build business from zero.

Acquisition is a merger of a business by acquisition of shares or assets of another company for the purpose of adding core capital. The acquisition strategy is an alternative business expansion that many companies do in the current era. Usually the acquirer company is a larger company than the company being targeted acquisition. In Indonesia, acquisitions began to flourish since the advancement of the capital market. Starting in 1980, Merger and acquisition activities showed a scale that increased significantly from year to year. The acquisition that occurred in Indonesia did not only occur locally, but also between countries. Since 1992 companies that have merged and acquired continued to increase, even if compared between 1996 and 1995 the increase in mergers and acquisitions increased to 67%. Basically, acquisition is a phenomenon that is known and developed not only in Indonesia, but almost all parts of the world in line with the development of the business world.

According to Pramadi (2013), Data from KPPU Indonesia shows companies that total companies that made acquisitions during the 2011-2013 periods were 101 companies followed by the next following year, 2014-2016, the total companies that made acquisitions rose to 164 companies. With the increasing acquisition action, this proves that more companies want to create business synergies with other companies and also to achieve efficiency and effectiveness. Besides bringing benefits, the decision of an acquisition is inseparable from the problem, including the cost of carrying out an acquisition is very expensive, and the results are also uncertain as expected. Moreover, the implementation of an acquisition can also has a negative influence on the financial position of acquiring companies if the structuring of the acquisition involves payment by cash and through a loan. Another problem is the possibility of a corporate culture, so it influences the human resources to be employed.

A popular approach to assessing the financial condition of a company is to evaluate accounting data in the form of financial statements because financial statements are prepared based on the standard of financial report and are widely applied by companies. Financial performance is very important for companies especially for goes public companies. Go public companies are companies owned by the community so that it is required to improve its performance in order to strengthen its capital based and to increase its prestige in the market. By going public, the companies will make the acquisition easily happen. The difference that occurs after a company makes an acquisition is the company's financial performance that increases or decreases. This change in financial performance will be reflected in the financial statements which include the calculation and interpretation of financial ratios. The increasing financial performance of the company will make the company highly competitive. On the contrary, the company's financial performance that is declining will make the company unable to compete. Increased financial performance is the achievement of the acquisition decision made, and contrary if the financial performance decreases, the decision to make an acquisition is wrong.

The way to find out the financial performance of a company can be done by analyzing its financial statements. The better the quality of the financial statements presented, the more convincing the external parties will be in looking at the company's financial performance. The financial statements are analyzed to identify each weakness of the financial situation that can cause problems in the future, and determine some strength that can be an advantage of the company.

The calculation of financial statement in a company can be measured by various types of analysis tools, which is ratio analysis. Some variables used by writer to assess financial performance include profitability, liquidity, company activity ratios, market value ratio, and leverage. Changes that occur after a company makes an acquisition will usually appear on the company's financial performance. The assessment of the success of the acquisition depends on several things, such as accurate assessment of the target company and making estimates of future prospects. The synergy generated by acquiring companies can increase over a long period of time, if the company uses resources effectively.

Based on several previous studies where there were differences in the results of research on the effects of mergers and acquisitions, where some researchers mentioned a significant difference and there were several researchers mentioned that there were no significant changes, which significant changes can be seen from the company's financial performance. The difference outcome of the previous studies as well as the motivational theory views of acquisition resulted in differences between theory and reality in empirical data from the average performance of companies that do an acquisition.

In this paper, the writer wants to elaborate whether the acquisition gives significantly differences on the parent entity or even no significantly differences on the parent entity after acquisition by analyzing the financial statement using financial ratios. Based on the preliminary study, the writer is interested to do the final paper entitled **"Comparative Analysis of Financial Performance Before and After Acquisition on the Company Listed on the Indonesia Stock Exchange (Empirical Study of Companies that made Acquisitions in 2014-2016)".**

1.2 Problem Limitation

Limitation of the problem is done so that the problems studied are more focused on the research objectives. Therefore, the following restrictions are made in this study, as follows:

1. The observation period was carried out in 2012-2018
2. The companies are not from financial or banking sector
3. Performance appraisal in this study is based on the company's financial performance and is measured by indicators of financial ratios obtained from published financial statements, include: Net Profit Margin (NPM), Total Asset Turnover (TATO), Debt to Equity Ratio (DER), Current Ratio (CR), and Earning per Share (EPS).
4. Analysis of differences in financial performance is carried out two years before and two years after the acquisition.

1.3 Problem Identification

Based on the background study above, the writer would like to identify the problem in acquisitions, which is as follow:

1. Is there a difference in the liquidity ratio as measured by the company's current ratio before and after acquisitions?
2. Is there a difference in the activity ratio as measured by the company's total asset turnover before and after acquisitions?
3. Is there a difference in the profitability ratio as measured by the company's net profit margin before and after acquisitions?
4. Is there a difference in the solvability ratio as measured by the company's debt to equity ratio before and after acquisitions?
5. Is there a difference in the market value ratio as measured by the company's earnings per share before and after acquisitions?

1.4 Objectives of the Research

The objectives of the research are:

a. To find out whether there is a difference in the company's liquidity ratio as measured by the current ratio before and after acquisitions.
b. To find out whether there is a difference in the company's activity ratio as measured by the total asset turnover before and after acquisitions.
c. To find out whether there is a difference in the company's profitability ratio as measured by the net profit margin before and after acquisitions.
d. To find out whether there is a difference in the company's solvability ratio as measured by the debt to equity ratio before and after acquisitions.
e. To find out whether there is a difference in the company's market value ratio as measured by the earnings per share before and after acquisitions.

1.5 Benefit of the Research

In a research, it is expected to be able to give something useful, while the benefits that researchers expect from this study are as follows:

1.5.1 Theoretical Benefit

The benefits of theoretical research are expected to be able to provide useful scientific contributions in the academic world regarding the effects of acquisitions on the financial performance of companies in Indonesia. This research is expected to be a comparative material, and development for future research in similar fields or problems.

1.5.2 Practical Benefit

The benefits of practical research can be used as a recommendation and consideration for investors in investing in the company, as well as a benchmark for investors to see the growth of the company. This research can be one of the references in returning decisions in choosing mergers and acquisitions as a corporate strategy.

1.6 System of Writing

In order to be more directed and systematic for the writing of this study, then a systematic writing is arranged as follows:

Chapter I: Introduction

This chapter explains about the introduction to the research. It explores the background of the study, the problem limitation, the problem formulation, objectives of the research study, benefits of the research study, and its systems of writing.

Chapter II: Literature Review and Hypothesis Development

This chapter explains the theoretical background of this research that will be used as a basis in processing data from companies. This chapter contains an understanding of business combination, form of business combination, classification of acquisition, motivation in acquisition,

acquisition process, problems arising in acquisition practices, understanding of company performance, understanding of financial statements, and understanding of financial ratios, previous research, framework of thinking, and hypothesis.

Chapter III: Research Methodology

In this chapter mentions about space scope of research, population, samples and sampling techniques, data sources, data collection methods, operational definitions and measurement of variables and methods of data analysis. This research is a descriptive study conducted under the quantitative approach using secondary data with companies which do an acquisition in 2014-2016, listed on the Indonesia Stock Exchange as population. The samples are taken by using non-probability sampling method that is purposive sampling method.

The quantitative research method in this study uses comparative research. The analysis technique is carried out by making comparisons between the same elements (financial statements) for several consecutive periods in 2012-2018. Data analysis methods used in this study includes normality tests, and paired sample t-test.

Chapter IV: Data Analysis and Discussion

This chapter contains descriptive statistics of research data, data analysis, normality testing of data as a result of testing hypotheses and discussion of the results and how they relate to the theories and previous researches.

Chapter V: Conclusion

In this chapter, the research conclusions are explained followed by the implications, and recommendations for future research.