P: ISSN No. 0976-8602 RNI No.UPENG/2012/426228 VOL.-IV, ISSUE-II, January-2015
E: ISSN No. 2349-9443
Asian Resonance

Creating Value Through Acquisitions: A Case Study of Arcelor Mittal

Abstract

Mergers and Acquisition are among the most efficient strategies for companies which results in operating synergy from either economies of scale or from improved managerial practices and financial synergy, lowering the cost of capital of the combined firms, reducing transaction-related costs associated with issuing new securities, and better matching of opportunities with internally generated funds. This study with the help of secondary sources, and short run analysis provides some starting point for the future researches to be made by policymakers in the case of mergers and acquisitions. The Arcelor-Mittals merger and acquisition delivered mixed results. It improved the profitability but very little. The measures on profitability such as ROS, ROA and ROE declined in the short-run analysis after merger, thus there were no significant improvements verified despite increase in net income. The measures on capital investment spending such as CESA and CETA showed insignificant declines after merger. At the time, leverage measures showed similar result in which debt to asset and debt to equity ratios all showed no improvements after M&A. The findings in relation to solvency of Arcelor-Mittal also showed no improvements in current ratio and working capital ratio in the short-run analysis after M&A of Arcelor-Mittal.

Keywords: Mergers, Acquisition, Operating synergy, Financial synergy, CESA, CETA.

Shashi Srivastava
Assistant Professor,
Department Faculty of Management,
Banaras Hindu University,
Varanasi.

Introduction

One of the most controversial business deals ever- the acquisition of Arcelor Steel by Mittal Steel led to the creation of Arcelor-Mittal, the largest steel maker in the world. Despite the fact that Mittal steel, the largest producer of steel in terms of volume is based in Netherlands, it is perceived that the company is non-European because its CEO Lakshmi Mittal is an Indian. Arcelor, Headquartered in Luxembourg, the merger of three steel companies- Aceralia, Arbed and Usinor led to the creation of Arcelor.

Research methodology

Research objectives

The objectives of the present Research are as follows

1. To study the impact of merger on profitability of combined entity after the Arcelor-Mittal deal.
2. To examine the impact of merger on solvency of combined entity.
3. To analyse the impact of merger on Operating efficiency of combined entity after the merger.

Research design

Research design is Exploratory in nature.

Data Collection

The required secondary data have been collected from financial statements of Arcelor(2003-05), Mittal Steel(2003-05) and Arcelor-Mittal(2006-10).

Data Analysis

The data have been analyzed through Ratio Analysis to judge the profitability, capital spending, leverage, solvency and operating efficiency of the two firms before merger and that of the entity after merger.

Statistical Significance

The independent sample t-test has been used to test for equality of means before and after merger.

P: ISSN No. 0976-8602 RNI No.UPENG/2012/426228 VOL.-IV, ISSUE-II, January-2015
E: ISSN No. 2349-9443
Asian Resonance

Data Analysis

Analysis of Financial Variables Before and After Merger

Profitability

Acquisition by merger and consolidation results in combination of the assets and liabilities of acquired and acquiring firms. Effects of merger in the financial performance using profits as the measure of success would lead one to conclude that on average merger will be a success.

Profitability		Pre-Merger	Post-Merger
	ROS – Net Income/Sales	0.06862	0.06064
	ROE – Net Income/Equity	0.20822	0.10645
	ROA – Net Income/Total Assets	0.06782	0.04847

Net Income

The mean Net income after the merger rose to 6159 million US dollars from the combined average net income of 938 million US dollars of Arcelor and 3061 million US dollars of Mittal. So it clearly shows the significant improvement in the average income after merger.

Return on Sales

Return on sales measures the profitability of the firm from its net income over its sales. Mean ROS for both Arcelor and Mittal has shown significant improvement after the merger.

Return on Equity

This ratio is used widely in the private sector to measure a firm's performance. This ratio measures returns relative to investments in the company. The mean ROE for Arcelor has gone up after merger whereas the mean ROE for Mittal has gone down significantly after the merger.

Return on Assets

It measures the profitability of the firm from its net income over its total assets. Firms with higher return on assets should be better able to raise money in security markets, because they offer prospects for better returns on the firm's investments. The mean ROA for Arcelor has gone up significantly after merger while mean ROA for Mittal has declined after merger.

Capital Spending

This measure shows the extent of the company's monetary investments in its fixed assets rather than in using it for its day-to-day operation.

Capital Spending		Pre-Merger	Post-Merger
	Capital Expenditure	2541.66	3426.4
	CESA – Capital Expenditure/Sales	0.04808	0.03632
	CETA – Capital Expenditure/Total Assets	0.04712	0.026

Capital Expenditure to Sales

The average Capital Expenditure to Sales (CESA) has decreased for both the companies after the merger.

Capital Expenditure to Total Assets

The ratio of Capital Expenditure to Total Assets (CETA) has decreased for both the companies after the merger.

Leverage

The leverage measure shows the extent that debt is used in company's capital structure. The debt to asset and debt to equity ratios are used in this paper to analyse the position of leverage before and after the merger.

Leverage		Pre-Merger	Post-Merger
	LEV1=Total Debt/Total Assets	0.25133	0.2228
	LEV2=Total Debt/Total Equity	0.83208	0.47492

Debt to Asset

The first measure of leverage is the ratio of debt to asset. For Arcelor There was a decrease in the debt to asset ratio after merger. This was basically due to low interest rates plus the significant efforts of the company to pay out debt that resulted in notable deduction of bank loans. The same has changed a very little for the Mittal.

Debt to Equity

The second measure of leverage is the ratio of debt to equity. There was a decrease in the debt to equity ratio for both the firms after the merger.

Liquidity

The liquidity measure shows how easily the company can use its cash when needed. It can be measured through Current Ratio, Acid Test Ratio and Working Capital to Total Asset Ratio.

Solvency		Pre-Merger	Post-Merger
	Current Ratio – Current Assets/Current Liabilities	1.48369	1.44831
	Acid Test Ratio – Quick Assets/Current Liabilities	0.82822	0.7249
	Working Capital to Total Asset ratio	0.14584	0.09937

Current Ratio

The first measure of short term solvency is the Current Ratio. The mean Current Ratio for Arcelor has shown a little improvement after the merger whereas for Mittal has gone down significantly after the merger.

Acid Test Ratio

The mean Acid Test Ratio for both the firms has gone down after the merger.

Working Capital to Total Asset Ratio

The ratio has gone down significantly on an average after the merger for both the firms.

Operating efficiency

Operating efficiency is the yardstick for the efficient usage of capital by the company. It can be measured by the Revenue and Depreciation.

Operating efficiency		Pre-Merger	Post-Merger
	Net Revenue	53803.8	91554.8
	Depreciation	2273.86	4617.4

Revenue

The first measure of operating efficiency is net revenue. The average Revenue after merger has increased for both the Arcelor and Mittal at a very high rate.

Depreciation

The second measure of operating efficiency is depreciation. This is an indicator of capital usage. There has been a significant rise in average depreciation for both the firms after the merger which shows that that capital usage has increased significantly after the merger deal has taken place.

Conclusion

The Arcelor-Mittals merger and acquisition delivered mixed results. It improved the profitability but very little. The measures on profitability such as ROS, ROA and ROE declined in the short-run analysis after merger, thus there were no significant improvements verified despite increase in net income The measures on capital investment spending such as CESA and CETA showed insignificant declines after merger. At the time, leverage measures showed similar result in which debt to asset and debt to equity ratios all showed no improvements after M&A. The findings in relation to solvency of Arcelor-Mittal also showed no improvements in current ratio and working capital ratio in the short-run analysis after M&A of Arcelor-Mittal. The operating efficiency used net revenue and depreciation measures. There was improvement noted in the two measures in the short-run analysis.

Significance of Study

Though the study suffers from limitations such as dependence on secondary sources, limited scope to study and short run analysis yet this study provides some starting point for the future researches to be made by policymakers in the case of mergers and acquisitions. It provides evidences as a basis for the steel industry's policymakers to formulate and implement laws that will help to improve the overall efficiency of the steel industry. Moreover, other remaining issues for the steel industry can be addressed in a separate study in the future. Issues for M&As in the steel industry are the effects of competition and productivity performance. Some important questions to be raised for future investigations are: What are the impacts of Arcelor-Mittals merger on other steel competitors? What are the effects or are there any significant changes on the productivity performance of the shipping industry following M&As? How does Arcelor-Mittal respond to its growing competitors both foreign and local? These are some other important issues that need to be addressed by future researchers. This study will serve as a gateway for further research concerning the impacts of M&A in the steel industry worldwide. Likewise, it will be useful to increase the number of countries involved in M&As in their steel industry and examine separately its impact on competition, productivity and efficiency performance. A separate study can also be done to examine the impact of Arcelor-Mittal merger and acquisition on the performance of other competing firms in the industry using market data, which are left for future investigation and acknowledged as limitations of the present study.

References

1. Basu, Ritu, Druck, Pablo, Marston, David and Susmel Raul (2004). 'Bank Consolidation and Performance: The Argentine Experience'. IMF Working Paper, Monetary and Financial Systems Department, WP/04/149, pp 1-32.
2. Bhan, Akhil (2009). 'Mergers in Indian Banking Sector – Motives and Benefits'. http://ssrn.com/abstract=1467813.
3. Jayadev, M and Sensarma, Rudra (2007). 'Mergers in Indian Banking – An Analysis'. https://uhra.herts.ac.uk/dspace/bitstream/2299/3465/1/902962.pdf.
4. Kemal, Muhammad Usman (2011). 'Post Merger Profitability: A Case of Royal Bank of Scotland'. International Journal of Business and Social Science, Vol. 2, No. 5, pp 157-162.
5. Mantravadi, Pramod and Reddy, A Vidyadhar (2008). 'Post-merger performance of Acquiring firms from different industries in India'. International Research Journal of Finance and Economics, ISSN 1450-2887 Issue 22, pp-192-204.
6. Sharma, Manu (2010). 'Determining value creation through Mergers and Acquisitions in the Banking industry using Accounting Study and Event Study Methodology, European'. Journal of Economics, Finance and Administrative Sciences, ISSN 1450-2275 Issue 19, pp 61-73.

P: ISSN No. 0976-8602 RNI No.UPENG/2012/426228 VOL.-IV, ISSUE-II, January-2015
E: ISSN No. 2349-9443
Asian Resonance

Appendix

Table -1

Figures (2003-05) (In $ Million)

	2003		2004		2005		Mean	
	Arcelor	Mittal	Arcelor	Mittal	Arcelor	Mittal	Arcelor	Mittal
Sales	30911.58	9567	34996.05	22197	35607.68	28132	33838.44	19965.33
Equity	8482.32	2561	9089.55	5846	14427.86	15457	10666.58	7954.667
Total Assets	32553.36	10137	33220.8	19153	36860.84	33867	34211.67	21052.33
Net Income	-234.36	1182	346.95	4701	2702.2	3301	938.2633	3061.333
Capital Expenditure	1782.9	421	1745.55	898	1596.54	1181	1708.33	833.333
Total Debt	10602.9	3067	8669.7	1980	7989.78	8308	9087.46	4451.66
Current Assets	16333.38	3683	16224.3	9625	18848.14	11355	17135.27	8221
Current Liability	12933.9	2619	11323.8	6230	12256.66	5599	12171.45	4816
Quick Assets	8683.92	2096	8803.35	5612	11965.2	5361	9817.49	4356.333
Revenue	30911.58	9567	34996.05	22197	35607.68	28132	33838.44	19965.33
Depreciation	1554.84	331	2161.35	553	1392.4	829	1702.863	571

Table -2

Figures For Arcelor-Mittal (2006-10) (In $ Million)

	Arcellor Mittal	Arcellor Mittal	Arcellor Mittal	Arcellor Mittal	Arcellor Mittal	Mean
	2006	2007	2008	2009	2010	
Sales	88576	105216	124936	65110	78025	92372.60
Equity	50228	61535	59230	65437	66100	60506
Total Assets	112681	133625	133088	127697	130904	127599
Net Income	7994	10368	9399	118	2916	6159
Capital Expenditure	136	5448	5531	2709	3308	3426.40
Total Debt	26567	30627	34076	24812	26008	28418
Current Assets	39413	45328	44414	32807	42675	40927.40
Current Liability	24560	32209	30760	23491	30723	28348.60
Quick Assets	20173	23578	19673	15972	23092	20497.60
Revenue	88576	105216	124936	61021	78025	91554.80
Depreciation	3448	4570	6100	4574	4395	4617.40

P: ISSN No. 0976-8602 RNI No.UPENG/2012/426228 VOL.-IV, ISSUE-II, January-2015
E: ISSN No. 2349-9443 Asian Resonance

Table -3
Analysis of Financial Variables

Profitability		Arcelor (2003-05)	Mittal (2003-05)	Arcelor- Mittal (2006-10)
	ROS – Net Income/Sales	0.02772	0.15333	0.06667
	ROE – Net Income/Equity	0.08796	0.38484	0.10179
	ROA – Net Income/Total Assets	0.02742	0.14541	0.04826
Capital spending				
	CESA – Capital Expenditure/Sales	0.05048	0.04173	0.03709
	CETA – Capital Expenditure/Total Assets	0.04993	0.03958	0.02685
Leverage				
	LEV1 – Total Debt/Total Assets	0.26562	0.21145	0.22271
	LEV2 – Total Debt/Total Equity	0.85195	0.55963	0.46967
Solvency				
	Current Ratio – Current Assets/Current Liabilities	1.40782	1.70701	1.44371
	Acid Test Ratio – Quick Assets/Current Liabilities	0.80667	0.90455	0.72305
	Working Capital to Total Asset ratio	0.14509	0.16174	0.09858
Operating Efficiency				
	Net Revenue	33838.44	19965.33	91554.80
	Depreciation	1702.86	571	4617.40

In January 2006, Mittal Steel launched a $22.7 billion offer to Arcelor's shareholders. The deal was split between Mittal Shares (75 percent) and cash (25 percent). Under the offer, Arcelor shareholders would have received 4 Mittal Steel shares and 35 euros for every 5 Arcelor shares they held. (Ultimately the power to buy or sell the shares rests with the shareholder and the company management can at best advice its shareholders whether to accept or reject the bid).

Independent Sample t Test of Arcelor Mittal

Financial Ratios	Assumption	T	Df	Sig. (2-tailed)
Profitability				
ROS – Net Income/Sales	Equal Variances	-0.273	6	**0.794**
ROE – Net Income/Equity	Equal Variances	-1.442	6	**0.199**
ROA – Net Income/Total Assets	Equal Variances	-0.727	6	**0.495**
Capital Spending				
Capital Expenditure	Equal Variances	0.663	6	**0.532**
Capital Expenditure/Sales	Equal Variances	-0.974	6	**0.368**
Capital Expenditure/Total Assets	Equal Variances	-2.052	6	**0.086**
Leverage				
LEV1=Total Debt/Total Assets	Equal Variances	-0.948	6	**0.380**
LEV2=Total Debt/Total Equity	Equal Variances	-2.223	6	**0.068**
Liquidity				
Current Assets/Current Liabilities	Equal Variances	-0.351	6	**0.738**
Quick Assets/Current Liabilities	Equal Variances	-1.440	6	**0.200**
Working Capital to Total Asset ratio	Equal Variances	-2.320	6	**0.059**
Operating Efficiency				
Net Revenue	Equal Variances	2.431	6	**0.051**
Depreciation	Equal Variances	3.947	6	**0.008(sig)**