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### RESEARCH ARTICLE

## IMPACT OF LEVERAGE BUYOUTS (LBO'S) ON THE SHARE PRICES OF THE ACQUIRING COMPANIES.

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#### Abstract

A leveraged buyout (LBO) is a transaction when a company or single asset is purchased with a combination of equity and significant amounts of borrowed money, structured in such a way that the target's cash flows or assets are used as the collateral (or "leverage") to secure and repay the borrowed money. In the changing scenario, leverage buyouts have been very common in India also. I have analyzed the impact of buyouts on the acquiring companies using abnormal returns and correlation method which gave positive results.

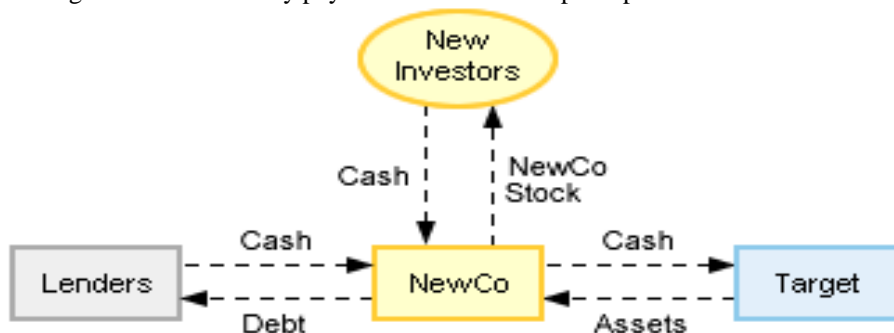
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#### Introduction:-

**Leverage buyouts** are the process by which a firm acquires another firm with the help of debts and equity. In leverage buyouts assets of the acquired company is used as a security against the loan taken by acquiring company. This helps the acquiring company to minimize their risk.

There are different forms of leverage buyouts such as management buyouts (MBO), management buy-in (MBI), secondary and tertiary buyouts, these can occur in growth situations, restructuring situations and insolvencies situations. Leverage buyouts involves institutional investors and financial sponsors who makes large acquisition, they also not commit all funds required for acquisition. Financial sponsor increases their returns by employing large amount of leverage (high ratio of debt to equity), they have an incentives to employ as much debt as possible to finance the acquisition.

Financial sponsor raises fund by issuing bonds or securing a loan, which is secured by assets of acquiring company or cash flow of the target as to make timely payment of interest and principal amount.



In case of huge transaction cost syndicate is also possible, which means more than one lender can join hand to pool the debt required for transaction on the other hand many financial sponsors can join hand to provide part of equity required for completing the transaction.

#### Objective:-

To analyze the share prices of the company's pre and post leverage buyout.

#### Research methodology:-

H0 = LBO's do not impact of share prices of acquiring companies from India.

H1= LBO's affect the share prices of acquiring companies from India.

The study is based on secondary data. The data of financial performance will be collected from different websites of the acquiring companies.

The data to analyze the share prices will be collected from the websites of BSE.

#### Data analysis:-

##### Abnormal return:-

##### Tata tea:-

|                      |                | Tata Tea        |
|----------------------|----------------|-----------------|
|                      |                | Abnormal Return |
| BSE Sensex           | 11 March, 2000 | -0.03255        |
|                      | 14 March, 2000 | 0.009064        |
|                      | 15 March, 2000 | 0.014307        |
| Company Share prices | 11 March, 2000 | 0               |
|                      | 14 March, 2000 | 0.07359         |
|                      | 15 March, 2000 | -0.00167        |

##### Interpretation:-

The date of acquisition was 10<sup>th</sup> March, 2006. The abnormal return of BSE sensex in 11 march, 2006 is decreased by -0.03255 means 3.255% but in case of company's share price it is 0 means abnormal return is impacted by LBO but on 14<sup>th</sup> march SENSEX abnormal return is 0.9064% but company' share price return is 7.359% means abnormal return is increased by comparing it with BSE sensex. On 15<sup>th</sup> march abnormal return on sensex is 0.014 and in case of company's

Share price it is -0.00167 means LBO impact the performance of the company means the performance in the 14<sup>th</sup> march is increased but on 15<sup>th</sup> march it is decreased means there is no any link with the sensex.

##### Tata steel:-

|                      |                 | Tata Steel      |
|----------------------|-----------------|-----------------|
|                      |                 | Abnormal return |
| BSE Sensex           | 21 October,2006 | 0.002157        |
|                      | 23 October,2006 | -0.00891        |
|                      | 24 October,2006 | 0.005952        |
| Company Share prices | 21 October,2006 | 0.016242        |
|                      | 23 October,2006 | -0.01394        |
|                      | 24 October,2006 | -0.01485        |

##### Interpretation:-

The date of LBO is 20<sup>th</sup> October 2006. The day after LBO means on 21<sup>st</sup> October the abnormal return of sensex is at 0.2% and of company's share price abnormal return is 1.6% but on 22<sup>nd</sup> October the abnormal return of sensex is at 0.891% and company's share price abnormal return is at 1.394%. On 23<sup>rd</sup> October abnormal return of sensex is at 0.5952% and abnormal return of company's share price is at 1.485%. It shows that the share price of the company is

not moving according to the sensex so LBO impact on the share price of the company. The performance of the company is decreased.

#### Ub group:-

|                      |             | ub group |
|----------------------|-------------|----------|
| BSE Sensex           | 17 may,2007 | 0.012203 |
|                      | 18 may,2007 | 0.000259 |
|                      | 19 may,2007 | 0.008053 |
| Company Share prices | 17 may,2007 | 0.156686 |
|                      | 18 may,2007 | -0.01272 |
|                      | 19 may,2007 | -0.0035  |

#### Interpretation:-

The acquisition was takes place on 16 may 2007. On that day the abnormal return of sensex was increased about 12% and company's share prices increased by 15% . Next day sensex increased but at lower rate like .02% but company's share prices fallen by 1.2% and again next day the sensex was increased but it was at high rate than previous day but still company's share prices was decreasing. So it shows there is effect of LBO on the company's share prices. And it is quite negative effect.

#### Suzlon energy:-

|                      |           | Suzlon Energy<br>Abnormal return |
|----------------------|-----------|----------------------------------|
| BSE Sensex           | 20-Mar-06 | 0.007452                         |
|                      | 21-Mar-06 | -0.003282                        |
|                      | 22-Mar-06 | -0.005855                        |
| Company Share prices | 20-Mar-06 | 0.007717                         |
|                      | 21-Mar-06 | -0.013401                        |
|                      | 22-Mar-06 | 0.014903                         |

This LBO was happened on 17 march in 2006. Then next two days stock market was off. On 20 march the abnormal return of sensex was increased by 0.7%. And company's share price was also increased about 0.8%. On 21 March the abnormal returns of SENSEX was decreased by 0.3% and company's share prices also decreased by 1.3%. But next day sensex was still falling but the shares prices was rised by 1.4%. It shows the share prices of company was not affected by sensex so here LBO has positive effect on the company's share prices because sensex is falling but company's share price is increasing.

#### Tata motors:-

|                      |          | Tata motors |
|----------------------|----------|-------------|
| BSE Sensex           | 1-Nov-07 | -0.0057284  |
|                      | 2-Nov-07 | 0.01277     |
|                      | 3-Nov-07 | -0.0192954  |
| Company Share prices | 1-nov-07 | -0.0177197  |
|                      | 2-Nov-07 | 0.01466149  |
|                      | 3-Nov-07 | -0.0200453  |

The LBO was happened on 31 October 2007. On next day the abnormal returns of sensex was decreased by 0.5% and company's share price was decreased by 1.7%. Again one day later the sensex rise by 1.2% and company's share price was rise by 1.4%. Again sensex fell by 1.9% and company's share price fell by 2%. It shows the changes in the share price of company were happened due to fluctuation in the sensex. So LBO has not any effect on the share price of company.

**Ub group:-**

| <b>Correlations:-</b> |                     |        |        |
|-----------------------|---------------------|--------|--------|
|                       |                     | Price  | Sensex |
| Price                 | Pearson Correlation | 1      | .788** |
|                       | Sig. (2-tailed)     |        | .000   |
|                       | N                   | 20     | 20     |
| Sensex                | Pearson Correlation | .788** | 1      |
|                       | Sig. (2-tailed)     | .000   |        |
|                       | N                   | 20     | 20     |

\*\* . Correlation is significant at the 0.01 level (2 tailed).

**Interpretation:-**

As per table number 11 which shows correlation between share price of UB group and sensex ,there is positive correlation (0.788)between sensex and share price .So there is impact of sensex on the share price of the company .There is increase in share price due to increase in sensex or vice versa.

**Suzlon:-**

| <b>Correlations</b> |                     |       |        |
|---------------------|---------------------|-------|--------|
|                     |                     | Price | Sensex |
| price               | Pearson Correlation | 1     | .656   |
|                     | Sig. (2-tailed)     |       | .002   |
|                     | N                   | 20    | 20     |
| sensex              | Pearson Correlation | .656  | 1      |
|                     | Sig. (2-tailed)     | .002  |        |
|                     | N                   | 20    | 20     |

**Interpretation:-**

As per table number 12 which shows correlation between share price of Suzlon and sensex ,there is positive correlation (0.656)between sensex and share price .So there is impact of sensex on the share price of the company .There is increase in share price due to increase in sensex or vice versa.

**Tata steel:-**

| <b>Correlations</b> |                     |         |         |
|---------------------|---------------------|---------|---------|
|                     |                     | Price   | Sensex  |
| price               | Pearson Correlation | 1       | -.772** |
|                     | Sig. (2-tailed)     |         | .000    |
|                     | N                   | 20      | 20      |
| sensex              | Pearson Correlation | -.772** | 1       |
|                     | Sig. (2-tailed)     | .000    |         |
|                     | N                   | 20      | 20      |

\*\* . Correlation is significant at the 0.01 level (2-tailed).

**Interpretation:-**

As per table number 13 which shows correlation between share price of Tata steel and sensex ,there is negative correlation (-0.772)between sensex and share price .So there is opposite impact of sensex on the share price of the company . There is increase in share price due to decrease in sensex or vice versa.

**Tata motors:-**

| Correlations |                     |       |        |
|--------------|---------------------|-------|--------|
|              |                     | Price | Sensex |
| price        | Pearson Correlation | 1     | -.158  |
|              | Sig. (2-tailed)     |       | .505   |
|              | N                   | 20    | 20     |
| sensex       | Pearson Correlation | -.158 | 1      |
|              | Sig. (2-tailed)     | .505  |        |
|              | N                   | 20    | 20     |

**Interpretation:-**

As per table number 14 which shows correlation between share price of Tata motors and sensex ,there is negative correlation (-0.158)between sensex and share price .So there is opposite impact of sensex on the share price of the company . There is increase in share price due to decrease in sensex or vice versa.

**Tata tea:-**

| Correlations |                     |       |        |
|--------------|---------------------|-------|--------|
|              |                     | Price | Sensex |
| price        | Pearson Correlation | 1     | .554*  |
|              | Sig. (2-tailed)     |       | .017   |
|              | N                   | 18    | 18     |
| Sensex       | Pearson Correlation | .554* | 1      |
|              | Sig. (2-tailed)     | .017  |        |
|              | N                   | 18    | 18     |

\*. Correlation is significant at the 0.05 level (2-tailed).

**Interpretation:-**

As per table number 15 which shows correlation between share price of Tata tea and sensex ,there is positive correlation (0.554)between sensex and share price .So there is opposite impact of sensex on the share price of the company . There is increase in share price due to increase in SENSEX or vice versa.

**Findings & Conclusion:-****Tata tea:-**

There is impact of leverage buyouts on the share price of the company and due to increase in SENSEX there is increase in share price of the company.

**Tata motors:-**

There is impact of leverage buyouts on the share price of the company but increase in sensex does not have positive impact on share price of the company.

**Tata steel:-**

There is impact of leverage buyouts on the share price of the company. There is also negative impact of increase in sensex on the share price of company.

**Suzlon:-**

There is impact of leverage buyouts on the share price of the company but there is positive impact of increase in sensex on the share price of company.

**UB group:-**

There is impact of leverage buyouts on the share price of the company but there is positive impact of increase in sensex on the share price of company.

**Conclusion:-**

We can say that due to leverage buyouts share of every company is affected, whereas when we tried to find out correlation between share price and sensex we found that some company has positive correlation where as some

company has negative correlation So we can say that increase or decrease in share price of some of the companies may be due to sensex or leverage buyouts but some companies have only impact of leverage buyouts.

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