

Corporate Focus and Shareholders Value creation : Evidence from Demerger Announcement

* **Dr Seema Singhal**

PURPOSE

One of the objective behind any strategic corporate decision is to maximize shareholder value. The present paper examines the announcement effect of 18 demergers on shareholders wealth in the short run during 1996-2006. The paper seeks to assess the impact of demerger announcement on the wealth of the demerged company's shareholders.

India. Unlocking or enhancing shareholders' value is the main reason for implementing a demerger. Companies that choose to implement a demerger believe that the value of their company when separated, will exceed the value of the all the companies. With shareholders' wealth maximization is the most important corporate goal, the study has made an in-depth analysis of pre-and post-demerger shareholders' wealth of eighteen demerged firms whose share price data have been available for the requisite period covered in the study.

Keywords: Demergers, Mergers and Acquisitions, Abnormal Return, Cumulative Abnormal Returns (CAR), Event Study, Media Announcement, Run-up Window.

Introduction

The growing tendency towards demergers world-wide has been driven by intensifying competition. The demerged companies expand business into new areas, attain global size, take benefit of economies of scale, invest quickly in technology for strategic gains, and improve shareholder value in this global competition. In India, demergers have increased significantly. Demergers is a strategic business decision and demerged company and its shareholders are expected to be the important beneficiaries of this decision. A popular belief is that Demerger make the strengthened and focused business. Demerged companies tend to improve their long term profitability through demerger route. Shareholders of the demerged firm also hope to make significant long term gains by investing in demerged company. Therefore, assessment of demerger activities has to be done keeping in mind these benefits. The present study aims at examining the short term impact of demerged companies in India in order to evaluate the efficacy of demerger strategy.

LITERATURE REVIEW

Chang and Hertz (2004)³⁷ in their paper investigated the relation between changes in firm value and changes in ownership structure that take place around non-control-related targeted repurchases of common stock for a sample of 223 target repurchases from 1979 to 1995. In contrast to the negative average abnormal return associated with the announcement of a control-related targeted repurchase (greenmail transaction), they found that the announcement of a non-control-related targeted repurchase is associated with a positive and significant average abnormal return. Cross-sectional analysis indicated that the change in firm value at the announcement of a non-control-related repurchase is negatively related to the resulting changes in both insider ownership and outside block-holdings. They also found significant differences in announcement-period stock price effects depending on the identity of the selling shareholder.

*Associate Professor, Department of Commerce, MDSD Girls College, Ambala City, Haryana, India,

Mishra and Goel (2005)³⁸ they examined the financial implication of RIL-RPL merger on the shareholders' wealth. The profitability for shareholders was investigated by examining the daily excess returns that accrue to the shareholders around the date of announcement of the merger deal. The study shows that positive excess return occurred to the shareholders of the target company RPL and negative excess returns to the shareholder of the acquiring company, RIL. They found that in this process of merger, despite the deal appearing to be favourable to the shareholders gained from the deal. This deal was led with the 'empire building' motive along with spreading the risk and return more equally among the shareholders of two companies.

Mallik and Rakshit (2006)³⁹ in their article examined and explained how a company restructures its business and increase shareholders value through demerger. It also seeks to discuss the importance of demerger as a business planning tool. Pre and post demerger financial performance evaluation under traditional method and EVA based method has also been attempted in this paper. The efficiency of strategic decision in ensuring over all value creation for an enterprise will be examined on the basis of case study of Dabur India Ltd They analyzed that under traditional performance measurement system ROCE is 9.2% i.e. the company earns profit from its investment and the company is value creating company. But the Hence from the post demerger financial performance analysis it appears that Dabur India Ltd.; performance is good but Dabur Pharma Ltd.; financial position is not good. The company recently entered into tie up with US based drug major to sell its oncology drugs. Ability to provide high quality products at reasonable / low prices is essential not only to combat competition and to emerge as Key player, but also to meet social goals.

NAG (2006)⁴⁰ explained in his article that companies like L & T and Reliance have demerged their entities which is beneficial to their shareholders. He discussed the process of demerged and how it impacts the shareholders' wealth. According to him demerger is the process of corporate restructuring in which a single or multiple business unit(s) is spun off as a new entity. Demerger is just the opposite of merger and tends to go in and out of fashion. When the market prices of shares are rising, the companies like to use their shares to acquire other companies. At this juncture, advisors of the company may suggest and encourage for a merger after taking over the other company. Where as in a falling market, mergers and initial public offers are less popular, and the merchant banks, which normally earn their fees from corporate activity, start looking at demerger possibilities of their clients. Demerger is not of recent origin. In the UK, Argos was spun out from British American Tobacco in 1990 and Zeneca was spun off from ICI in 1993. In India, the most prominent demergers in recent times include the cement division of L & T Ltd, named as Ultratech Cement Ltd, Reliance energy Ventures Ltd, Reliance Natural Resources Ventures Ltd, and Reliance Capital Ventures Ltd, - which spun out from RIL. While the demerger of Ultra tech from L & T seems to be one of L & T's grand strategies to concentrate more on Infrastructure, Engineering, Energy and Turnkey businesses, the demergers of RIL were the outcome of ownership settlements between two siblings (Promoters) in RIL. This demerger had two important issues. The first important issue was that L & T Employees Welfare Foundation was given a stake in the company; in a way, it protected the interests of both existing and former employees. While the second issue was that shareholders at large also got benefited from this demerger. During early 2003, L & T's Rs. 10 face value share prior to demerger was hovering around Rs. 350/400 per share. After the demerger, for every 100 shares of L & T, shareholders got 50 shares of L & T of Rs. 5 face value each and 40 shares of UCL with face value of Rs. 10 each. Around April 2004, the entire demerger process was complete. Initially there

were some corrections in the market. Later, share prices of both L & T and UCL started rising. Within two years, shareholders of erstwhile L & T have almost trebled their wealth with a growth more than SENSEX or Nifty. In the first week of April 2006, face value of Rs.5 a share of L & T was quoted at Rs.2432, while of UCL quoted Rs.683 per share. This means shareholders' value went up more than 100 % within two years, which was unprecedented in the history of demergers of any company.

Sudarsanam and Qian (2007)⁴¹ in their findings proposed and tested from a sample of 170 European spinoffs completed during the period from 1987 to 2005, the governance-based model for spin off value effects, which argued that spinoffs create shareholder value by enhancing corporate governance and mitigating agency costs in post-spinoff firms., they present some evidence supporting the governance-based hypotheses. First, they found that spinoff parents are likely to have weaker corporate governance than non-spinoff control firms. Therefore, agency problems in spinoff parents seem to be more severe than those in non-spinoff control firms. Second, they found the strength of corporate governance for spinoff parents is generally negatively associated with the spinoff announcement period abnormal returns although the relationship is insignificant. Third, they concluded that post-spinoff firms with increased board independence or facing takeover threats earn significantly higher long-run abnormal returns than those without such activities. Finally, they document evidence that family-controlled parent firms have significantly lower performance than non-family-controlled parent firms. Therefore, they evidence indicates that the gains from spinoffs reflect the lessening of agency conflicts.

Unyong (2007)⁴² in his article explored changes in compensation and pay-for-performance relationships for a sample of 124 spinoffs during 1990-1997. They concluded that the operating performance results support management incentive explanation over business focus as the source of value creation in spinoffs. Their findings suggested that changes in managerial incentive compensation are a significant motivation for corporate spinoffs. Corporate spinoffs enhance managerial incentive compensation and the changes in managerial incentive compensation explain the value enhancement and operating performance improvements 'that occur following spinoffs.' They reached a conclusion that the pay-performance relations improve following spinoff distributions in three aspects. First they found that PPS increases for spinoff subsidiaries but remains the same for the parent firms. Second, they advocated that PPS for spinoff subsidiaries does not decrease when a pre-parent's CEO becomes a spinoff subsidiary's CEO adjusting for size effects. Third, resulted the higher incentives are offered to the CEO of spinoff subsidiaries created from FI spinoffs than that of pre-parents involved in FI spinoffs. So the changes in managerial incentives are significant motives for corporate spinoffs. Firms appear to use spinoffs as a way to rewrite managerial compensation contracts more efficiently and to improve firm performance. While the managerial incentive hypothesis and the business focus hypothesis are not mutually exclusive, the results from operating performance show that the managerial incentive effect appears to dominate the business focus effect.

Lundh (2007)⁴³ in his project concluded that spinoffs are an increasing phenomenon on the Swedish stock market. He had observed 17 pre-spinoff companies that become 34 post-spin off companies which continued to be traded on the stock market. In this report one can read about factors that trigger spinoffs as well about the short and medium term risk and return that spinoffs yield. He compared the spinoff company and the parent company in the post-spinoff scenario it can be concluded that the company who is performing the best is also the riskier alternative and the spinoff performs better than the parent

company in eleven out of seventeen times. There is also a correlation between risk and return- when higher return is observed it also brings higher risk, and it holds true in all samples except one.

Veld and Merkoulouva (2008)⁴⁴ in their research reviewed the literature on the factors that influence the wealth effects associated with the announcements of corporate spin-offs. They used meta-analysis to summarize the findings of 26 event studies on spin-off announcements. They found a significantly positive average abnormal return of 3.02% during the event window. Returns are higher for larger spin-offs, for divestments that are tax or regulatory friendly and for spin-offs that lead to the divestiture of a non-related division. They also found that spin-offs that were later completed were associated with lower abnormal returns than non-completed spin-offs. They overviewed studies on the long-run stock price performance of spin-offs. Even though early studies found a long-run superior performance, this effect was no longer found in later studies that use more refined statistical tests.

Ramakrishnan (2008)⁴⁵ indicated that the long-term post-merger performance of 414 mergers between 1993 and 2005. He has carried out statistical analyses of financial data pertaining to 87 pairs of merged firms. These mergers took place in the period 1996 to 2002. It is found that the merged firms demonstrate improvement in long-term financial performance after controlling for pre-merger performance, with increasing cash flow returns post merger, at an annual rate of 4.3%. This improved operating cash flow return is on account of improvements in the post-merger operating margins of the firms, though not of the efficient utilization of the assets to generate higher sales. Increase in market power also appears to be driving gains through mergers in India. As far as wealth gains on merger announcement are concerned, only the shareholders of the acquired firms appear to be enjoying significant positive share price returns of 11.6%. The shareholders of the acquiring firms and the combined firms do not seem to be witnessing any significant change in returns. With regard to the strategic factors affecting long-term post-merger financial performance, related mergers seem to be performing 5.4% lower than unrelated mergers. Both the transfer of corporate control from the acquired firm to the acquiring firm, and the business health of the acquired firm are positively related to the long-term post-merger performance of the firms. In the case of mergers where there is a transfer of management control, none of these three groups of shareholders witnesses any abnormal returns on announcement of the merger. The wealth gains to acquired firm shareholders on announcement of a merger are positively influenced by the relative size and the pre-merger performance of the acquired firm. The transfer of corporate control from the acquired firm to the acquiring firm is negatively associated with these abnormal share price returns. The level of industry-relatedness of the acquired and the acquiring firms, the method of payment for the acquired firm and the business health of the acquired firm do not appear to be playing a role in affecting the share price returns to the acquired firm shareholders, on announcement of a merger.

Anand and Singh (2008)⁴⁶ they used event study methodology to analyze five mergers in Indian Banking Sector to capture the returns to shareholders as a result of the merger announcement during the period of 1999 to 2005. They explored the short-term shareholder wealth effects of the Indian Bank mergers. The merger of Times Bank with HDFC Bank (1999), The Bank of Madura with the ICICI Bank (2000), the ICICI Ltd. with ICICI Bank (2001), the Global Trust Bank (GTB) with the Oriental Bank of Commerce (OBC) (2004), and the Bank of Punjab (BOP) merger with the Centurian Bank (2005) have been studied. The findings of the study were in agreement with the European and the US bank mergers and acquisitions except for the fact that the value to the shareholders of the bidder banks has been destroyed in the US

context. From the study, it emerged that merger announcement in the Indian banking industry has positive and significant shareholders' wealth affect both for the bidder and target banks.

Raffaele Attruia (2014): The Creation of shareholders value through Spin-Offs : The case of YAHOO - The results of this study confirm that spin-off can have positive impacts in the short period, delivering higher value to its shareholders given the higher transparency of the two businesses. However in the long-run, the results depend on the capability of these two or more businesses to generate value on their own. The case study on Yahoo and its equity investment in Alibaba remains empirical evidence that, under certain conditions, spin-offs are a source of value creation.

Pavak Vyas (2015) : Impact of Demerger Announcement on Shareholder Value: Evidences from India This paper examines the demergers and the announcement period price reaction of demergers during the year 2012-2014. The authors have studied total 51 demergers of companies listed in India. Researcher has found out that significant out-performance of the security over the benchmark index post demerger announcement ranging from 1.74% average abnormal return for a demerger announcement to 0.16% average abnormal return 10 days following the announcement.

Bendre Mahesh and Apte Nehra (2017) concluded that cases of demergers in Indian corporate world are increasing in recent times. Majority of the spin- offs that have taken place in India are associated with objective of overall value creation for the shareholders. The researcher has identified and studied 24 spin-offs that took place in India during 2012-2017. The result of this study has shown that demerger activity has an overall positive effect on shareholder wealth. The most favourable time for share-holder wealth creation remains to be from demerger announcement date to the listing of demerged entity. During this phase, 80% of the cases have given 49% average returns. However during the demerger announcement date and demerger effective date, only 60% of total stocks have given positive returns with 18% increase in average market capitalization. This behavior may reflect the uncertainty regarding the regulatory outcome and shareholders' approval for the spin-off proposal from the Company.

Methodology: This paper applies an event study methodology to empirically test the effect of announcement of Demergers using daily stock returns. The study applies regression analysis with secondary data examining 18 companies.

EVENT STUDY

Event study start with hypothesis that particular event affects the value of a firm. The hypothesis that the value of the company has changed will be translated in the stock showing abnormal return. Coupled with the notion that the information is readily impounded into prices, the concept of abnormal returns (or performance) is the central key of the event study methods.

Window Period and Clean Period Data

Seiler (2004) explained that event study is composed of three frames.

1. Estimation Window (- 240 to -41)
2. The Event Window (-40 to +40)
3. Post Event Window (41 to 240)

Estimation Window

The estimation window is used to determine the normal behaviour of the stock market factors. Most often used formulae is $R_{it} = \alpha + \beta R_{mt}$ to determine the normal window. The estimation window is also used to determine the normal behaviour of stock's return with respect to a market of industry index. The

estimation of the stock's return in the estimation window is required to define a model of normal behaviour. This estimation window is used to calculate risk and return of demerged companies.

Event Window

The event window often starts a few days before the actual event day. The length of the event window is centered on the announcement and is normally one, three, five, ten, fifteen, twenty-five and forty days. This procedure enables the researcher to investigate present leakage of the information.

Post Event Window

It is used to investigate longer-term company performance following the announcement of the event such as demerger and merger. It is to measure the long term impact of the event. The post event window can be as short as one month and as long as several years depending on the event. The event window in the research has been taken from -40 days to the date of announcement to 40 days. The clean period data for the demerged company has been taken as 200 days before -40 days window and 200 days after the 40 days window period.

Window Period	Clean Period	
	Before Demerger	After Demerger
-40 to 40 days	-240 days to -41 days	41 days to 240 days

The share price data and market index (BSE 200) has been taken from Prowess 3.1 the database Software developed by CMIE and from National stock Exchange.

Estimating CAR Using the Market Model

Fama and MacBeth (1973) market model assumes that all interrelationships among the returns on individual assets arise from a common market factor that affects the return on all assets. The following model generates the expected returns on individual assets. In order to capture the systematic abnormal price movements that are interpreted as prima facie evidence of market's reaction to announcement of an event (firm demerger in this case), the risk and market adjusted variant of standard event study methodology which is better known as the market model has been employed, and it is depicted as follows:

$$R_{it} = \alpha_j + (\beta_j * R_{mt}) + \varepsilon_{it}$$

t = -240 to -41 (estimation window/period)

The residual return has been calculated for each security by deducting actual return on a particular day during the study period 40 day's window under market model from the predicted returns, as follows:

$$r_{jt} = R_{jt} - (\alpha_j + \beta_j * R_{mt})$$

Where r_{jt} = Abnormal Return for company stock j at time t

R_{jt} = Actual Return for company stock j at time t

α_j = The intercept term which measure the return over a particular period not explained by market or ordinary least squares (OLS) estimate of the intercept of the market model regression.

β_j = Measures the risk of the security or the sensitivity of firm j's return to that of market or ordinary least squares (OLS) estimate of the slope of the market model regression.

R_{mt} = The return on the BSE 200 index on the day t.

ε_{it} = The unsystematic component of firm j's return.

Furthermore, the daily average abnormal returns (AR_t) of demerger announcement in a 40 days window are estimated for demerged company by taking arithmetic average of the residual returns of respective companies of that group.

$$AR_t = \frac{\sum r_{it}}{N}$$

AR_t = Average abnormal returns of demerger announcement

N = Number of firms in the sample.

The reason for averaging across firms is that stock returns are noisy but the noise tends to cancel out when averaged across a large number of firms. Therefore, more firms in the sample, the better ability to distinguish the effect of an event. The cumulative average returns (CAR) of demerger announcement in a 40 days window are estimated for demerged companies by submission of the average abnormal returns (AR_t) in the respective window

$$CAR = \sum_{t=-40}^{40} AR_t \quad t = -40 \text{ to } 40$$

Where CAR = Cumulative Average Abnormal Returns of demerger announcement.

$$t - \text{statistics of Abnormal Returns} = \frac{r_{jt}}{S(r_j)}$$

Where $S(r_j)$ = Standard deviation of residual of company j for the clean period.

$$t - \text{statistics of Average Abnormal Returns} = \frac{AR_t}{S(AR)}$$

Where $S(AR)$ = Standard deviation of average abnormal returns of demerged company during clean period.

$$t - \text{statistics of } CAR = \frac{CAR}{\sqrt{CAR} \sqrt{t}}$$

Where t = respective window period.

Statistical Significance of Event Returns

The null hypothesis that there are no abnormal returns associated with the demerger announcement needs to be statistically tested. The statistical significance of the daily residual returns of each company (r_{jt}), daily average abnormal returns (AR_t) of demerged and cumulative abnormal return (CAR), has been examined using the t- statistic. If the estimated value of t-statistic is greater than 1.64 but less than 1.96, it is significant at 10% level. If estimated value of t statistics is greater than 1.96 and less than 2.58, it is significant at 5% level. If its value exceeds 2.58, it is significant at 1% level. In the event of the t-statistic being significant, it implies that there are abnormal returns associated with the demerger announcements in India. The results of the event study using market model with respect to company demerger announcement are as under. These results are based on the data given in the annexure V.

Sample Selection and Period of Study

To analyze the impact of demerger announcement on the shareholder wealth these 18 Demergers in the Indian Corporate Sector during the period 1996 to 2006 have been studied. The detailed information about the demerged companies is given in Table1.

Event Definition and Date of Announcement

For the purpose of this study the first date of media announcement of the demerger has been taken as the event date (day zero). Table1 enumerates the date of announcement of the Demergers. The first possible date when the news of the merger was made public has been used. The same has been obtained from PROWESS 3.1; the data based software developed by Center for Monitoring Indian Economy (CMIE)., web sites of Securities and Exchange Board of India (SEBI), Bombay Stock Exchange (BSE) and National Stock Exchange (NSE). Table1 shows the abbreviation of the companies used in the study and their first media announcement date.

Table1-Event Date of Announcement of Demerged Companies

Sr. No.	Company Name	Company Name	First Media Announcement date
1.	CEAT LTD	CEAT	MAY 18, 1999
2.	CROMPTON GREAVES LTD	CROMPT	JULY 7, 2000
3.	DABUR INDIA LTD	DABUR	AUGUST 9, 1999
4.	GODREJ INDUSTRIES LTD	GODREJ	AUGUST 1. 2000
5.	GRASIM INDUSTIES LTD	GRASIM	JANUARY 7, 2000
6.	HMT LTD	HMT	JULY 16,1999
7.	INFOSYS TECHNOLOGIES LTD	INFO	JUNE 30, 2000
8.	J.K.SYNTHETICS LTD	JKSYNT	OCTOBER 14, 2002
9.	KESORAM INDUSTRIES LTD	KESO	JULY 7, 2000
10.	KODAK INDIA PRIVATE LTD	KODAK	NOVEMBER1, 1999
11.	LARSON AND TOUBRO LTD	LARSON	JANUARY 19, 2000
12.	NIRMA LTD	NIRMA	JUNE 30, 2000
13.	RAYMOND LTD	RAYMD	MAY 25, 1999
14.	STEEL AUTHORITY OF INDIA LTD	SAIL	DECEMBER 8,1999
15.	TATA COMMUNICATION LTD	TATA	OCTOBER 21, 1999
16.	VOLTAS LTD	VOLTAS	JUNE 19, 2000
17.	WIPRO LTD	WIPRO	AUGUST 19, 1999
18.	ZEE ENTERTAINMENT ENTERPRISES LTD	ZEE	JULY 5, 1999

Table2 gives the date wise data used for clean and window periods for the demerged companies.

Table2-Clean Period & Window Period Data for Demerged Companies

Sr. No.	Name of Company	Data Available for Clean Period (-240 to -41)		Data Available for Window Period (-40 to 40)	
		Start Date	End Date	Start Date	End Date
1.	CEAT	May 25, 1998	March 11,1999	March 12, 1999	July 12,1999
2.	CROMP	July 22, 1999	May 11, 2000	May 12,2000	Sept 5,2000
3.	DABUR	Oct.22, 1998	June10, 1999	June11,1999	Sept 28,1999
4.	GODREJ	Aug.20, 1999	Feb.10,2000	Feb11,2000	May 8,2000
5.	GRASIM	March15, 1999	Nov 10,1999	Nov 11,1999	Feb 28,2000
6.	HMT	May 26, 1998	May 19, 1999	May 20, 1999	Sept 14,1999
7.	INFO	July 15, 1999	May 4, 2000	May 5, 2000	Aug 28, 2000
8.	JKS	Oct.29, 2001	Aug13, 2002	Aug 14,2002	Dec 12, 2002
9.	KESO	July 22, 1999	May 11, 2000	May12, 2000	Sept 5, 2000
10.	KODAK	Nov.13, 1998	Sept.1, 1999	Sept.2, 1999	Dec 29,1999
11.	LARSON	Feb.2, 1999	Nov.19, 1999	Nov. 22,1999	March16,2000
12	NIRMA	July15, 1999	May4, 2000	May 5, 2000	Aug 28, 2000
13.	RAYMD	June 2, 1998	March22, 1999	March23,1999	July22,1999
14	SAIL	Dec.18, 1998	Oct 7, 1999	Oct 8,1999	Feb 4, 2000
15.	TATA	April 27, 1998	Aug 23, 1999	Aug 24,1999	Dec 20,1999
16.	VOLTAS	July 2, 1999	April 19, 2000	April 20, 2000	Aug 14,2000
17.	WIPRO	Aug.27, 1998	June.22, 1999	June23,1999	Oct.14,1999
18	ZEE	July1 3,1998	May7, 1999	May10,1999	Aug30,1999

Summary Statistics of Demerged Companies

The summary statistics provides the detail of regression results for estimating the expected return during window period. Table4 lists the summary statistics of demerged companies. In all we have calculated the following and tested their significance level.

- Alpha (α)

- Beta (β)
- Standard Deviation
- t-statistics
- CAR
- CAAR

The following table shows the summary statistics of demerged companies. These are calculated by using clean period data that is 200 days before -40 days window.

Table3-Summary Statistics of Demerged Companies

Company Name	α	β	Std deviation
CEAT	-0.0022	1.4559	0.0276
CROMPT	-0.0046	0.9827	0.0416
DABUR	0.0035	-0.0527	0.0355
GODREJ	0.0002	0.1108	0.0496
GRASIM	0.0059	-0.2467	0.0407
HMT	0.0006	-0.1078	0.0849
INFO	0.0059	1.2735	0.0361
JKSYNT	-0.0001	0.8630	0.0579
KESO	-0.0027	0.9584	0.0463
KODAK	0.0008	0.6177	0.0316
LARSON	0.0015	1.2937	0.0256
NIRMA	-0.0016	0.9527	0.0399
RAYMD	-0.0035	1.3192	0.0387
SAIL	-0.0024	1.7194	0.0492
TATA	-0.0035	1.3192	0.0387
VOLTAS	-0.0043	-0.0680	0.0390
WIPRO	0.0026	0.9656	0.0303
ZEE	0.0031	1.2641	0.0291

Cumulative Average Abnormal Returns Estimates during the Window Period

The estimates of cumulative abnormal returns of the demerged companies in the different windows are reported as under.

As revealed by Table 4, the average CAR of the demerged companies is positive and substantial as we move from one-day window to two day to five-day window wherein it has decreased from 1% to 3.8% to 3.1%. Further it has increased in 10-day window and 25 day window i.e. 4.8% and 4.5%. In 1 day CAR is significant at 1% level of significance and 2 day window CAR is significant at 10% level of significant. Combined CAR in the entire window period 1, 2, 5, 10, 15, 25 and 40 is positive.

Table4-Cumulative Average Abnormal Returns of all the Selected Demerged Companies

Window	CAAR	Days	t-statistics	Percentage of CAR
CAR 1 Day Window	0.051*	03	3.038	5.1
CAR 2 Day Window	0.038***	05	1.768	3.8
CAR 5 Day Window	0.031	11	0.976	3.1
CAR 10 Day Window	0.048	21	1.079	4.8
CAR 15 Day Window	0.026	31	0.474	2.6
CAR 25 Day Window	0.045	51	0.646	4.5
CAR 40 Day Window	0.025	81	0.290	2.5
Run up window				
(-1 Day)	0.007	01	0.718	.7
(-2 TO -1 Day)	0.018	02	1.297	1.8
(-5 TO -1 Day)	0.027	05	1.264	2.7
(-10 TO -1 Day)	0.053***	10	1.731	5.3
(-15 TO -1 Day)	0.070***	15	1.854	7
(-25 TO -1 Day)	0.045	25	0.923	4.5
(-40 TO -1 Day)	0.077	40	1.247	7.7
After announcement				
(+1 Day)	0.018***	01	1.892	1.8
(+2 TO +1 Day)	-0.005	02	-0.376	.5
(+5 TO +1 Day)	-0.022	05	-1.003	2.2
(+10 TO +1 Day)	-0.031	10	-1.007	3.1
(+15 TO +1 Day)	-0.070***	15	-1.857	7
(+25 TO +1 Day)	-0.078	25	-1.597	7.8
(+40TO +1 Day)	-0.077	40	-1.253	7.7

*denotes Significant at 1% level, ** denotes Significant at 5%, *** denotes Significant at 10%

In the run up window CAR in One day before is 0.7%. It moves up to 0.7% to 1.8% to 2.7% to 5.3% and finally in 40 day before it reaches to 7.7%. The CAR of 10 day and 15 day before window is significant at 10% level. Combined CAR is negative after announcement. One day after announcement CAR is 1.8% and it is significant at 10% level of significance. 10 day after announcement CAR is negative and continuously increasing from 3.1% to 7.8% and 7.7% in after 25 day and 40 day respectively. In nutshell we can conclude that demerger create wealth to the shareholders in short window. The combined CAR shows positive but significant only in one-day window at 1% after Demerger. On the whole demerger has created shareholder wealth in short window after demerger.

Statistical Significance of Cumulative Average Abnormal Returns

The statistical significance of CAAR in Single factor model is given in Table5

Table5-Statistical Significance of Cumulative Average Abnormal Returns

Window	CAAR	%of CAAR	t-statistics
Day before announcement (-1)	0.0070	0.70	0.7182
Day of demerger announcement (0)	0.0257*	2.57*	2.6523
Day after demerger announcement (+1)	0.0184***	1.84***	1.8922
Day before demerger announcement to the day of announcement (-1 to 0)	0.0327*	3.27*	3.3705
Day before demerger announcement to the day after announcement (-1 to +1)	0.0511*	5.11*	5.2627

*denotes Significant at 1% level, ** denote Significant at 5%, *** denote Significant at 10%

CAAR of all demerged companies is positive and significant in short window. CAAR of one day before announcement is 0.7% that is not statistically significant. On announcement day it is 2.57%, which is statistically significant at 1% level of significance. One day after demerger it is 1.84%, which is statistically significant at 10% level. CAAR in day before announcement to the day of announcement (-1, 0) is 3.27% significant at 1% level. Its value on the day before announcement to the day after announcement (-1, +1) is 5.11% that is statistically significant at 1% level. In nutshell demerger has created shareholders wealth after demerger because CAAR after announcement of demerger is positive substantial as statistically significant.

Conclusion

The objective of this paper is to investigate the announcement effect of demerger on Indian demerged companies shareholders wealth in the short run. A sample of 18 Indian acquiring firms has been analyzed in order to find empirical evidence that whether the announcement of demerger generate value for acquirer and its shareholders in India, during the period 1996-2016.

To analyse the abnormal returns to acquiring shareholders over a period of forty days surrounding the announcement day with different event windows, the event study methodology was applied. The objective of choosing a short event period, under which the returns of the stocks are examined, is that there will be no information other than the news of the demerger during this period, and the observed returns should therefore be entirely due to this news.

This study finds that the announcement of demerger generate significant positive value for acquiring firm shareholders in India in the short run. The empirical results obtained from the event study methodology suggest that demerged companies' shareholders receive a substantial significant and positive average abnormal return around the announcement day of demerger only. The findings of this study suggest significant and positive abnormal returns on both of the days prior to the announcement day. The positive abnormal returns on the days in the event period that are prior to the announcement day may have been seen be due to dispersal of news of some of the demerger before the actual day of announcement, which often occur due to rumours. In nutshell, demerged companies shareholders experience positive average abnormal return immediately following the announcement day. However, Demerger has created shareholder wealth in short window after demerger. In nutshell demerger has created shareholders wealth after demerger because CAAR after announcement of demerger is positive substantial and statistically significant.

References

1. Mehrotra Vikas, Mikkelson Wayn, Partch Megan (2003): The Design of Financial Policies in Corporate Spin-offs, The Review of Financial Studies, winter 2003; 16, 4; ABI/INFIRM Global pp 1359-1388.
2. Kohtamaki Marko, Kekale Tauno and Riitta Viitala (2004): Trust and Innovation: from Spin – Off Idea to Stock Exchange, Creativity and Innovation Management, Vol.13, Number 2 June, pp 75 – 86.
3. Kumar Rajesh (2004): Effect of RPL-RIL Merger on Shareholders' Wealth and Corporate Performance, The ICFAI Journal of Applied Finance, September, pp 13-34.
4. Veld C and Veld Merkoulova Y V (2004): Do Spin- Offs Really Create Value? The European Case, Journal of Banking and Finance, Vol. 28, No. 5, May, pp 1111-1135.
5. Chang Saeyong and Hertzel Michael (2004): Equity Ownership and Firm Value: Evidence from Targeted Stock Repurchases The Financial Review 39, pp 389 – 407.
6. Mishra A.K. and Goel Rashmi (2005): Returns to Shareholders from Mergers: The Case of RIL and RPL Merger IMB Management Review, September pp 69 -79.
7. Malik K.Amit and Rakshit Dabdas (2006): Corporate Restructuring through Demerger: A Case Study, Journal of Finance India (December) Vol. XX No.4 pp 1321– 1338.
8. Nag G.C. (2006): Demerger: A Boon for Shareholders' Market Value, Effective Executive, July, pp 63 -71.
9. Sudarsanam Sudi and Qian Binsheng (2007): Shareholder Value Gains from European Spinoffs: The Effect of Internal and External Control Mechanisms, JEL Classification: G 34, pp 1 – 47.
10. Unyong Pyo (2007) Enhancing Managerial Incentives and Value Creation: Evidence from Corporate Spinoffs Journal of Economics and Finance Vol.31, Number 3, pp 341 – 358.
11. Lundh Hampus (2007): Corporate Spinoffs: A Risk and Return Perspective, Bachelor Thesis in Finance, Jonkoping International Business School, January, pp 1-32.
12. Veld Chris and Veld Yulia V. & Merkoulova (2008): Value Creation through Spin-Offs: A Review of the Empirical Evidence, website ssrn.com, pp 1 – 28.
13. Ramakrishanan K (2008): Long term Post-Merger Performance of Firms in India, Vikalpa, Volume 33, No. 2, April-June, pp 47-62.
14. Anand Manoj and Singh Jagandeep (2008): Impact of Merger Announcement on Shareholders' Wealth: Evidence from Indian Private Sector Banks, Vikalpa, Vol. 33, No. 1, January-March, pp 35-54.
15. Raffaele Attruia (2015):The Creation of Shareholder Value Through Spin-Offs: The Case Of Yahoo,Luiss Guido Carli, Libera Universita Internazionale Degli Studi Sociali, Department of Business And Management,Master Thesis In M&A And Investment Banking.
16. Mahesh Bendre, ²Dr. Netra Apte(2016):Study of impact of spin-offs on shareholders wealth in India, international research journal of multidisciplinary studies, vol 3, issue 10, october, 2017.