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The Significance of Mergers and Acquisitions of Banks to Performance: Evidence from Nigeria

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Abstract
In an attempt to reposition the Nigerian banking sector and move the nation's economy forward, the then Central Bank of Nigeria Governor, Professor Charles Soludo, came up with a landmark consolidation policy. The options open to Nigerian banks to beef up their capital base were to capitalize their reserves, raise fresh funds from the capital market or embark on mergers and acquisitions which appear the most appealing and most feasible. The objectives of the study therefore were to examine the state of Nigerian banks before mergers and acquisitions, to assess the quality of the Nigerian banking sector after the mergers and acquisitions of banks and to investigate the significant relationship between mergers and acquisitions of banks and the performance of Nigerian banks. Data were collected through primary source and the method adopted in analyzing the data included t-test statistic and correlation analysis. The study found that there is a significant difference between the performance of banks before and after the introduction of mergers and acquisitions and that there is a significant relationship between mergers and acquisitions and bank performance in Nigeria.
Keywords: Mergers and Acquisitions, Consolidation, Capital Base, Capital Market, Banking Sector, Perfomance, Central Bank of Nigeria

1 Introduction

The Nigerian banking sector has undergone remarkable changes over the years, in terms of the number of institutions, ownership structure, as well as the depth of operations. These changes have been influenced largely by challenges posed by deregulation of the financial sector, globalization of operations, technological innovations and adoption of supervisory and prudential requirements that conform to international standards. Meanwhile, the wave of mergers and acquisitions that recently swept through the banking sector started after the announcement by the Central Bank of Nigeria (CBN), that banks in Nigeria should beef up their minimum capital base to N25 billion on or or before 31st December, 2005. As the terminal date for banks' consolidation workout was drawing nearer, desperate efforts were made by banks to meet the minimum capital fixed by the CBN before the expiration date. There were many options available towards solving the challenges of recapitalization; a bank could among other options, merge with another or with others or acquire smaller ones or volunteer to be acquired by a bigger one or stand alone or go for a combination of two or more of the options. Nevertheless, the strategies adopted by majority of these banks were mergers and acquisitions. Mergers and acquisitions therefore brought about a fusion of 69 banks while 6 opted to stand alone and 14 were to go for liquidation. The end result was that the then 89 banks in the country shrunk into 25 mega banks initially. These 25 banks have now been reduced to 20 of late.

Agusto (2004) notes that mergers or acquisitions, an attempt towards consolidation, is simply another way of saying survival of the fittest that is to say, a bigger, more efficient, better-capitalized, more skilled industry is part of the natural evolution of industries. It is primarily driven by business motives and/or market forces and regulatory interventions. Through financial intermediation, banks facilitate capital formation (investment) and promote economic growth. The banking industry in Nigeria has witnessed a remarkable growth, especially since the de-regulation of the financial services sector in the last quarter of 1986. In terms of headcount for instance, the number of banks increased by about154.8% from 42 in 1986 to 107 in 1990. It further increased by about 12% to120 in 1992. By 2004, however, the number had reduced to 89. This was because some banks had to be liquidated on account of their dwindling fortunes. The number of bank branches also rose from 1,394 in 1986 to 2,013 in 1990; 2,391 in 1992 and by 2004 in spite of the report published by Canadian Centre of Science and Education of 149 reduction in number of banks branches, it had swollen to 3,100 which translated into an inter-temporal increase of 44%, 18.8% and 29.7%, respectively (Ebong, 2006). Recapitalization in the banking industry has raised much argument among the bank regulators and to a large extent, this consolidation (mostly by mergers and acquisitions) was based on the proposition that there will be gains accruing from expenses reductions, increased market power, reduced earnings volatility and encouragement of the economies of scale.

1.1 Statement of the Problem

Business organizations are recently seeing mergers and acquisitions as an alternative means of re-capitalizing. Notably, in all human endeavours, there are bound to be successes and failures, and the Nigerian banking industry has proven to be no exceptions to this. The distress syndrome which had crept into the Nigerian banking sector since the early 1990s has persisted and this has brought about chronic systemic crisis. Although the consolidation policy which was largely exhibited through the medium of mergers and acquisitions seemed to have led to enhanced capital base for the banks in Nigeria as well as transforming them into strong players in regional and global banking environment, the extent to which this wave of bank mergers and acquisitions has transformed the sector and boosted the confidence of the customers, the investors and the shareholders' needs to be assessed. The ability of the banks to increase their market power and take full advantage of the benefits accruing to mergers and acquisitions of organizations which ultimately enhances the performance of the banks especially through the financing of the real sector of the Nigerian economy is not in doubt. The research work therefore seeks to investigate and evaluate the significance of mergers and acquisitions to bank performance in Nigeria.

1.2 Objectives of the Study

-To examine the state of Nigerian banks before mergers and acquisitions.
-To assess the quality of the Nigerian banking sector after the mergers and acquisitions of banks
-To investigate the significant relationship between mergers and acquisitions of banks and the performance of Nigerian banks.

1.3 Research Hypotheses

Hypothesis 1

-The introduction of mergers and acquisitions has no significant difference on bank performance before and after the consolidation policy.

Hypothesis 2

-There is no significant relationship between mergers and acquisitions of banks and the performance of Nigerian banks

1.4 Literature Review and Theoretical Framework

1.4.1 *Conceptual Framework*

Mergers and acquisitions are a global business terms used in achieving business growth and survival. Mergers entail the coming together of two or more firms to become one big firm, while acquisitions is the takeover or purchase of a small firm by a big firm; which are both pursuing similar motives (Gaughan, 1999; Amedu 2004; Bello 2004; Katty 2005). Accordingly, Soludo (2004) opines that mergers and acquisitions are aimed at achieving cost efficiency through economies of scale, and to diversify and expand the range of business activities for improved performance. Akhamiokor (1989) defines acquisitions as a business combination in which ownership and management of independently operating enterprises are brought under the control of a single management. A merger has been statutorily defined in the Company and Allied Matters Act (1990) as amended, in Section 590, as an amalgamation of the undertakings or interest in undertaking of one or more companies and one or more corporate bodies. The Act also defines acquisitions as a take-over by one company of sufficient shares in another to give the acquiring company control of the other company. By the statutory definition stated in Section 590 of the Act, a merger involves absorption of the whole undertaking of the acquired company (Acquiree) in the acquiring company (Acquiror). Business combinations which may take forms of mergers, acquisitions, amalgamation and take-over are important features of corporate structural changes. They have played important role in the external growth of a number of leading companies in the world.

However, Kay (1993) opines that mergers and acquisitions often form part of the strategic options expected to transform company performances. While in mergers, both merging firms lose their registration to becoming a new company entirely. Acquisitions involve the stronger organization swallowing the smaller or weaker one entirely without the stronger changing its identity. Merger is simply the metamorphosing of two independent firms with different names into one single business entity emerging from the agreement. Mergers actually has the capacity of bringing about synergy.

1.4.2 *Literature Review*

Numerous studies have empirically examined whether mergers and acquisitions are the solution to bank problems. The studies of Cabral, Dierick & Vesala (2002), Carletti, Hartmann & Spagnolo (2002) & Szapary (2001) provide the foundation for a research on the linkage between banks mergers and acquisitions and profitability. Evidence as provided in Calomiris & Karenski (1998), De-Nicolo (2003), & Caprion (1999) suggest that mergers and acquisitions in the financial system could impact positively on the efficiency of most banks. Surprisingly, the available empirical evidences suggest that mergers and acquisitions operations in the United State banking industry have not had a positive influence on performance in terms of efficiency (DeLong & DeYoung 2007; Amel, Barnes, Panetta & Salleo 2004; Berger, Demsetz & Strahan 1999). On the overall, these studies provide mixed evidence and many fail to show a clear relationship between mergers and acquisitions and bank performance.

Some of the previous literature have examined the impact of mergers and acquisitions operations on the cost efficiency as measured by simple cost accounting ratios (Rhoades, 1990, 1993; Pilloff, 1996; De Long & De Young, 2007), the impact on cost X- efficiency (Berger & Humphrey, 1993; De Young, 1997; Peristiani, 1997; Berger, 1998; Rhoades, 1993). Healy, Palepu & Ruback (1992) examine all commercial banks and bank holding company mergers and acquisitions between 1982 and 1986. They find that mergers and acquisitions did not reduce non- interest expenses that could lead to improved efficiency. According to Pilloff & Santomero (1998), there is little empirical evidence of mergers and acquisitions achieving growth or any other important performance gains.

However, Cornett & Tehranian (1992) & Kay (1993) found some evidence of superior post merger period because of the merged firms' enhanced ability to attract loans. They also show increased employee productivity and net asset growth. Also, this is evident in the Nigeria's banking industry (Okpanachi, 2006). Walter & Uche (2005) posited that mergers and acquisitions made Nigerian banks more efficient. Similarly, Uchendu (2005) & Kama (2007) opine that bank consolidation, which took place in Malaysia, facilitated banks' expansion that led to growth. In a related study of the Chilean banking industry, Kwan & Eisenbeis (1999) found 1hat the high rate of economic activities experienced in Chile was mainly from productivity's improvement of the large banks formed as a result of mergers and acquisitions which suggests that there may be more substantial scale efficiencies from larger sizes of banks as a result of mergers and acquisitions. But for Straub (2007), mergers and acquisitions have often failed to add significantly to the performance of the banking sector. Surprisingly, the majority of studies comparing pre and post mergers performance found that these potentials for efficiency derived from mergers and acquisitions rarely materialize (Pilloff, 1996; Berger, Demsetz & Strahan 1999). Towards this end, Beitel, Schiereck & Wahrenbur (2003) find no gain effect due to mergers and acquisitions, but for Yener & David (2004), mergers and acquisitions played an important role in improving after-mergers financial performance, which is a stimulus for efficiency. Most of the studies found that mergers and acquisitions add significantly to the profits of the banking sector except for Straub (2007) & Rhoades (1993) that hold contrary views.

1.4.3 *Theoretical Framework*

Many theories have emerged to explain the need for mergers and acquisitions. However, it is pertinent to realize that the motives for mergers and acquisitions are complex and they present challenges of classification. Also, there are numerous reasons for mergers and acquisitions, and these are succintly highlighted in diverse theories below.

(a) Efficiency Theories

This theory holds that mergers and acquisitions have good potentials for social benefits. They generally involve improving the performance of incumbent management or achieving a form of synergy. These theories will now be considered separately in order to clearly differentiate them and because each by itself, may explain certain classes of mergers.

(i) Differential Managerial Efficiency

This is the most general theory of mergers and acquisitions that can be formulated. In everyday language, such a theory operates where the management of firm A is more efficient than the management of firm B and if after firm A acquires firm B, the efficiency of firm B is brought up to the level of efficiency in the acquiring firm. Differential efficiency would most likely be a factor in mergers between firms in related industries where the need for improvement could be more easily identified thus, it is more likely to be a basis for horizontal mergers.

(ii) Operating Synergy

This theory assumes that economies of scales exist in the industry and that prior to the merger; the firms are operating at levels of activity that fall short of achieving the potentials of economies of scale. It included the concept of complementary capabilities. Operating Synergy may be achieved in horizontal, vertical and even conglomerate mergers. For example, one firm might be strong in research and development (R&D) but weak in marketing while another has a strong marketing department without the R&D capability. Merging both firms will result in operating synergy.

(iii). Financial Synergy

This theory hypothesizes complementariness between merging firms, not in management capabilities, but in the availability of investment opportunities and internal cash flows. A firm in a declining industry will produce large cash flows since there are few attractive investment opportunities. A growing industry has more investment opportunities than cash with which to finance them. These conditions will provide a basis for merging. The merged firm will have a lower cost of capital due to the lower cost of internal funds as well as possible risk reduction, savings in floatation costs and improvements in capital allocation.

(b) Agency Problems and Managerialism

Agency problems may result from a conflict of interest between managers and shareholders or between shareholders and debt holders. A number of organizations and market mechanisms serve to discipline self-serving managers and mergers and acquisitions are viewed as the discipline of last resort. Managerialism on the other hand, views mergers and acquisitions as a manifestation of the agency problem rather than its solution. It suggests that self-serving managers make ill-conceived combinations solely to increase firm size and their own compensations.

(c) The Free Cash Flow Hypothesis

Jensen (1986) hypothesis states that mergers and acquisitions arise because of large agency costs associated with conflicts between managers and shareholders over the payout of free cash flow that is in excess of investment needs. According to him, shareholders and managers have serious conflicts of interest that can never be resolved perfectly. When these costs are large, mergers and acquisitions can help to reduce them.

(d) Market Power

One reason often given for a merger or acquisition is that it will increase a firm's market share. Essentially, there appears to be a high degree of correlation between increased market share and increased profitability. This view is closely aligned to the economies of scale argument; since increasing market share usually entails a higher level of production, economies of scale will be achieved. Increasing market share by mergers and acquisitions might entail investigation by the anti-trust authorities because they are seen to result in undue concentration.

2 Methodology

This study made use of primary data and the entire banking sector in Nigeria was the study population. However, 5 representing 25% of this population were selected as the sample size Structured questionnaires were randomly administered to 70 respondents drawn from the selected 5 out of the 20 existing banks in Nigeria. The respondents were however stratified into senior management and junior management. A total of 14 staff were selected from each of the 5 banks comprising 4 senior management staff and 10 junior management staff randomly and in all, 60 of the questionnaires were duly filled and retrieved.

3 Techniques of Data Analysis

The techniques of data analysis were basically centred around hypotheses testing. e techniques adopted were paired sample t-test statistic which was used to test hypothesis 1 while correlation analysis was used to test hypotheses 2.

3.1 Hypotheses Testing

Hypothesis 1:The introduction of mergers and acquisitions has no significant difference on bank performance before and after the consolidation policy.

Pairwise T-test Statistic

Variable	N	Mean	Standard Deviation	Crit-t	Cal-t	DF	P
Mergers and Acquisitions	60	27.8458	5.94863				
Bank Performance	60	37.5292	5.13654	1.96	17.114	59	.004

Source: Author's Computation, 2014

The table above showed that the introduction of mergers and acquisitions has significant difference on bank performance before and after recapitalization (Crit-t =1.96, Calc-t=17.114, df=59, P<0..01 level of significance since the value of P stands at P=.000). The result is significant at 1 per cent since the critical value for t was greater than the tabulated value. The result however shows that the mean falls in 27.8458 and 37.5292.The null hypothesis which indicates that the introduction of mergers and acquisitions has no significant difference on bank performance before and after recapitalization is rejected.

Hypothesis 2: There is no significant relationship between mergers and acquisitions and bank performance

Pearson's Correlation Technique

Variable	N	Mean	Standard Deviation	R	P	Remarks
Mergers and Acquisitions	60	27.8458	5.94863		0.00	Significant at 1%
Bank Performance	60	37.5292	5.13654	-.599(**)		

Source: Author's Computation, 2014

The result from the table above shows that the mean value of 27.8458 for mergers and acquisitions and 37.5292 for bank performance falls within the minimum and maximum values of 25.00 and 91.00 and 17.00 and 48.00. The result also shows a low standard deviation of 5.94863 and 5.13654. However, based on the result from the correlation table, there is an indication that correlation is significant at the 0.01level with a 2-tailed test. This result indicates that P<0.05 since P =0.00 with the correlation value being -.599 (**). Hence it is significant at 5%. Based on the outcome of therefore, it can be concluded that there is a significant relationship between mergers and acquisitions and bank performance thus the null hypothesis is rejected.

3.2 Empirical Analysis
-The introduction of mergers and acquisitions has a significant difference on bank performance before and after the consolidation policy in Nigeria
- There is a significant relationship between mergers and acquisitions and bank performance in Nigeria

4 Conclusion
This paper reviewed the significance of mergers and acquisitions to bank performance in Nigeria. It examined the state of the banking industry before the introduction of mergers and acquisitions as a way out of the low capital base in which the sector has found itself. The study also assessed the quality of Nigerian banks after the 2004 recapitalization policy. The study adopted a survey research method by administering structured questionnaires to the sampled respondents. Two basic hypothesis were tested in an attempt to investigate the significant difference between the performance of banks before and after the introduction of mergers and acquisitions into the Nigerian banking sector and also to explore the relationship between mergers and acquisitions and bank performance. The null hypothesis for each of the two tested hypotheses were rejected Consequently, the study found a significant difference between bank performance before and after the introduction of mergers and acquisitions. It also revealed a relationship between mergers and acquisitions and the performance of Nigerian banks.

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Appendix

Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Standard Deviation
Mergers and Acquisitions	60	25.00	91.00	52.4125	5.94863
Bank Performance	60	17.00	48.00	37.5292	5.13654
Valid N (leastwise)	60				

Correlations

		Mergers and Acquisitions	Bank Performance
Mergers and Acquisitions	Pearson Correlation	1	-.599 (**)
	Sig.(2-tailed)		.000
	N	60	60
Bank Performance		-.599 ((**)	1

Paired Samples Statistics

	Mean	N	Standard Deviation	Standard Error
Pair Mergers and Acquisitions		60	5.94863	. 38398
Bank Performance		.60	.5.13654	.33156

Paired Samples Correlations

	N	Correlation	Sig.
Pair Mergers and Acquisitions	60	-.247	.000
Bank Performance			