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Corporate Restructuring through Mergers and Acquisition: Experience from Nigeria

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Abstract

This paper examines corporate restructuring in Nigeria with emphasis on mergers and acquisition. It started by reviewing the history of mergers and acquisitions and went further to theoretically assess the implications of mergers and acquisitions for economic growth. The foray into history revealed very few mergers and acquisitions in the years prior to bank consolidation (2004- 2005). The unprecedented numbers of mergers and acquisitions during bank consolidation prompted the adoption of this period in the assessment of the impact of mergers and acquisitions on banks' performance. To achieve this, the study compared the pre and post consolidated performance of banks using seven years before (1997-2003) and seven years after (2004-2010) bank consolidation in Nigeria in the analysis. The study concludes that Nigerian banks performed slightly better after consolidation.

Keywords: Mergers, acquisition, bank performance, consolidation

1. Introduction

Mergers and acquisitions are known to be popular means of corporate restructuring. They play important role in growth of many leading companies in the world and national economies. On the part of the firms, they serve as mechanisms for maximization of the firms' share of the market to enhance profitability and ultimately increase the market value of the firm's shares. Also, they provide economic and financial benefits, such as, economies of scale, risk diversification, ability to compete locally and internationally. To the national economy, mergers and acquisitions as means of corporate restructuring bring about structural adjustment which enables vast economic resources to move more quickly to their highest valued use. In the process, substantial benefits and competitive environment have been created.

In addition, both developed and developing economies require new technologies for economic growth. Corporate restructuring through mergers and acquisitions could also lead to the speedy adoption and/or transfer of new technologies. Technological change is an economic good and is the driving force of long-term economic growth. Since mergers and acquisitions are instrumental to technological change, they serve as engines of growth in both developed and developing economies.

In Nigeria, there were no successful mergers and acquisitions in the real sector of the economy until 1983 – 1996. Even then, the impact was not felt. Only few foreign firms in Nigeria merged in this period. Between 2004 and 2005, the wave of mergers and acquisitions was high though mainly in the banking sector (Acha, 2006). This process of corporate restructuring seems to have remained a strategy for structural adjustment to achieve growth, particularly in the banking sector. This has raised the concern to investigate the effect of merger and acquisition on the performance of banks in Nigeria. The specific objectives of the study are: to examine mergers and acquisitions in Nigeria and to assess the effect of mergers and acquisitions on the assets of banks in Nigeria.

2. Theoretical Framework

Summary of ideas and theories influencing the study are presented in this section. The relevant conceptual issues, theoretical literature and explanations of the relationship between merger, acquisition and economic growth are discussed. These include the concepts of mergers and acquisition; the theories of growth; mergers, acquisition and economic growth; the trend of mergers and acquisitions in Nigeria.

2.1 The Concepts of Merger and Acquisition

Mergers and acquisitions are the most common ways of undertaking corporate restructuring. The restructuring involves ownership, business and assets. Through mergers and acquisitions ownership of the company may change; business may be reorganized in terms of units and divisions, diversification into new ventures and

change of management; assets restructuring may involve sales of assets, sale and lease back of assets, and securitization. The ultimate purpose of the restructuring is to enhance the shareholder value.

(a) Merger

Merger occurs when two or more companies combine into one. Akamiokhor (1995); defines merger as combination or fusion of two or more formerly independent business units into one organization with a common ownership and management. Pandey (2010) explains merger in terms of amalgamation. According to Pandey, "laws in India use amalgamation for merger". Section 2(1A) of the Income Tax Act, 1961 in India defines amalgamation as the merger of one or more companies. The companies merged are the amalgamating companies and the new company formed is the amalgamated company. Section 590 of the Nigerian Companies and Allied Matters Act 1990 defines merger as "any amalgamation of the undertakings or any part of the undertakings of one or more companies and one or more bodies corporate".

Merger could also occur through the process of absorption. Absorption is a combination of two separate business entities in which the business of one of the merging companies is transferred to another and the transferred company is voluntarily wound up (Kalu, 1995). For example, in Nigeria, Standard Trust Bank Nig. Plc. merged with United Bank for Africa (UBA) in 2005 and Standard Trust Bank lost its identity to UBA. Another way merger could occur is through consolidation. This is combination of two or more companies into a new company. In this form of merger, all companies are legally dissolved and new entity is created. All companies involved transfer their assets, liabilities and shares to the new company. A typical example of this is the merger of nine banks to form Unity bank (see table 2) which was a completely new identity as none of the merged banks went by that name.

Types of Merger

- Horizontal Merger

This is the joining of two or more firms in the same area of business. Firms classified under this category perform similar functions in the production or sale of comparable products. The peculiar feature in this type of merger is that the amalgamating companies were competitors prior to the amalgamation. However, horizontal mergers may still be subdivided into either market extension or product extension mergers. Market extension merger may not lessen competition. In this type of merger, attempt is made to extend the market geographically. On the other hand, product extension horizontal merger is one in which the amalgamated firm enjoys the advantage of extended product line.

- Vertical Merger

This is combination of two or more firms involved in different stages of production or distribution, for instance, merging the business of a Rubber Plantation Company and a Tire Producing Company. Vertical merger may take the form of backward and forward integration.

- Conglomerate Merger

Conglomerate merger is the form of merger where firms engaged in different types of business activities have come together. In financial context, conglomerates merger tends to imply a union of business units with little or no product or market similarities. The products of the combining firms are unrelated and therefore do not compete for buyers or for raw materials prior to the amalgamation.

(a) Acquisition

An acquisition is the purchase of one organization by another. It could be through friendly bid or hostile bid. It is friendly, when the management of the acquiring firm and the target firm work out suitable terms that are agreed to by both firms. The company that makes friendly take-over offer to the target company is referred to as "yellow knight". On the other hand, it is hostile when the bid is such that the target firm resists. Here, the company that makes a hostile takeover offer on a target company is known as a black knight".

Jenson and Fama (1994) defines acquisition as an act of acquiring effective control over assets or management of a company by another company without any combination of businesses or companies. In acquisition, two or more companies may remain independent separate legal entities but there may be change in control of the companies. An acquirer may be a company or persons targeting to hold substantial quantity of shares or voting rights of the Target Company or gaining control over the target company.

2.2 Assessment of Value Creation through Mergers and Acquisition

It makes economic sense to the merging firm or acquiring firm if the shareholder's benefit increases. Economically advantageous value is created through mergers and acquisitions when the combined present value of the merging firm or acquiring firm is greater than the sum of their individual present values as separate

entities. Presented mathematically, if firm X and Y merge or X is acquiring Y; their respective worth are expressed as Wx and Wy, while the worth of the merged or acquiring firm would be Wxy. The economic advantage will occur if:

$Wxy > (Wx + Wy)$. This implies that:

$EA = Wxy - (Wx + Wy)$

Where:

EA = Economic Advantage

Wx = Worth of Firm x

Wy = Worth of Firm y

Since merger or acquisition involves costs, the net economic advantage is determined as below:

$NEA = [Wxy - (Wx + Wy)] - (C - Wy)$

Where:

NEA = Net Economic Advantage

C = Cost of merging or acquisition

Another method of assessing value creation in merger and acquisition is the Discounted Cash Flow (DCF) approach. Merger and acquisition is investment with expectation of future stream of incomes. It will therefore be beneficial if the present value of the target merger or acquired firm over a period is greater than the cost of merger or acquisition. To determine this, discounted cash flow technique becomes inevitable and the analyst must consider estimation of cash flows over a period, estimation of the value of cash flow beyond the period and the discount rate.

According to Rappaport (1979), the following steps are involved in the valuation of merger and acquisition;

- Identification of growth and profitability assumptions
- Estimation of cash flow and terminal value
- Estimation of the cost of capital
- Computation of present value of cash flows
- Decision if the acquisition is attractive on the bases of the present value.
- Decision if the acquisition should be financed through cash or exchange of shares.
- Evaluation of the impact of the merger on earning per share and price-earnings ratio.

This aspect of assessment is often handled by experts, usually financial analysts. However to calculate the minimum amount acceptable and maximum amount payable to shareholders, the procedures include:

(i) Computation of the value of the company being taken over prior to the takeover.
(ii) Computation of the value of the company taking the other over prior to take over.
(iii) Computation of the post-acquisition value of the enlarged company after acquisition.

The minimum sum to pay the shareholders of the company being taken over is the value computed in (i) above while the maximum amount to pay to shareholders of the company being taken over is value computed in (iii) less value computed in (ii) above.

2.3 Mergers, Acquisitions and Economic Growth

Corporate restructuring through merger and acquisition is a global issue but common in industrialized countries. They have played important role in the world vis-a-vis their respective economies. They are recognized all over the world as mechanisms for maximization of company's share of the market to enhance profitability and ultimately increase the market value of company's share. In addition, they provide financial and fiscal gains such as economies of scale, risk diversification, taxation, improvement of equity base, increase in earnings per share, access to rare management talent and employment opportunities.

Mergers and acquisitions help economies to adjust to major competitive changes among alternative management teams and organizational structures for control of corporate assets. This enables vast economic resources to move more quickly to their highest valued use. In the word of Jenson (1988):

> *Economic analysis and evidence indicates that merger and acquisition play important role in economic growth and has made substantial benefits for the shareholders. Overall gains to selling firm shareholders from mergers, acquisitions and other corporate restructuring in the 12 year period from 1977 through 1988 total over*

> *$500 billion. I estimate gains to buying firm shareholders to be at least $50 billion for the same period. These gains equal 53 percent of the total cash dividends (valued in 1988 dollars) paid to investors by the entire. Mergers and acquisitions are a response to new technologies or market conditions that require a strategic change in a company's direction or use of resources. Pp. 21 - 48*

He further claimed that publicly held corporation has outlived its usefulness in many sectors of economies over the world. New organizations through merging and acquisition and other going-private transaction are manifestation of this change. A central source of waste in the public corporation is the conflict between owners and managers over free cash flow. This conflict helps explain the prominent role of debt in the new organizations. The new organization's resolution of the conflict explains how they can motivate people and manage resources more effectively than public corporations (Jenson, 1988).

In line with Jenson's views, Ball *et al* (2004) sees combinations of firms in the form of mergers and acquisitions as strategic alliances aimed at achieving faster market entry and start-up; gain access to new products, technologies and markets; and share costs, resources and risks. In his words:

> *Swedish ASEA and Swiss Brown Bovari both energy generation and transmission specialists merged to form an $18 billion company. The reason according to CEO of the new firm was that the two firms individually were too small to compete with US and Japanese rivals as Wasting House, General Electric, Hitachi and Toshiba. Sandoz, a Swiss pharmaceutical manufacturer acquired Gerber for $3.7 billion in order to double the size of its food products division. Two years later, Sandoz and Ciba Geigy, another Swiss drug company, merged to form Novartis, which would then become the second largest pharmaceutical firm in the world Pp. 90-91.*

Mergers and acquisitions are not recent developments. Five periods of high merger activity known as merger waves have occurred in USA. The periods are; 1897 – 1904, 1916 – 1929, 1965 – 1969, 1984 – 1989 and 1993 – 2000 (Alao, 2010). Till today merger and acquisition is still a strategy for corporate restructuring to achieve internal growth of companies and the economic growth.

In India, about 1180 proposals for amalgamation of corporate bodies involving about 2,400 companies were filed with the high courts during 1976 – 1986. In 2003 – 2004, 834 mergers and acquisition deals took place, aimed at growth of the amalgamating companies and the entire economy (Bhattacharyya, 1988).

The experience of merger and acquisition became popular in Nigeria, particularly, in the banking sector during consolidation process in 2004 and 2005. Nigerian banks adopted several strategies to achieve the stipulated minimum capital base of ₦25 billion. Merger and acquisitions were the most widespread corporate strategies used by many banks to form mega banks and afford the minimum capital base (Akintoye and Somoye, 2008). These actions were propelled by the need to deepen the financial sector and reposition the sector for growth. Merger and acquisition enabled the banks to penetrate into new markets, gain technical and management expertise and knowledge as well as efficient allocation of resources. The mega banks are penetrating deeply the Nigerian Stock Exchange thereby impacting on the Nigerian economy.

3. The Trend of Mergers and Acquisitions in Nigeria

The first successful merger in Nigeria was that between A. G. Leventis and Company Limited and Leventis Stores Ltd in 1983, but the most celebrated merger was that between Lever Brothers Nigeria Ltd – a quoted company and Lipton Nigeria Ltd – a private company in 1984 (Akinsulire, 2008:567; http://wwwglobal businessinsights.com/content/rbfs0063m.pdf).

Other successful mergers and acquisition in the real sector of the Nigerian economy are included in table 1:

Insert table 1

The wave of merger and acquisition from 1983 – 1996 was not significant, and had little impact on the real sector of the economy. It is noted that only 11 firms were merged and acquired for a period of 13 years. This was quite unlike mergers and acquisitions in the banking sector between 2004 and 2005. Within the short period,

many banks merged or were acquired, causing an unprecedented wave of business combinations and restructuring. The component members of merged or acquired banks are listed in table 2.

Insert table 2

3.1 The Effect of Mergers and Acquisition on Bank Performance in Nigeria

In assessing the effect of merger and acquisition on bank performance in Nigeria, asset of banks is used as proxy for bank performance. Comparative analysis is the method used for the examination. The asset of banks prior to adoption of merger and acquisition is compared to asset of banks in the post era of adoption of merger and acquisition. Time series data on bank assets from 1997 – 2003 (prior to adoption of merger and acquisition) and 2004 – 2010 (post era of adoption of merger and acquisition) are used for the comparative analysis. Tables and simple percentages are the tools of economic analysis applied.

Insert table 3A & 3B

In table 3A (total asset of banks prior to adoption of merger and acquisition) the average growth rate of total assets of banks is 29% while that of 3B (total assets of banks after adoption of merger and acquisition) is 31%. Average growth rate of assets in post era of adoption of merger and acquisition is only 2% higher than the average growth rate of assets before adoption of merger and acquisition in the banking sector. Though the difference is very insignificant, it is clear that in 2006, the growth rate of bank assets was as high as 59%. This was as a result of the concentration in merger and acquisition in 2005. Throughout the period under review, the growth rate of total bank assets prior to adoption of merger and acquisition was insignificant. In the post-merger and acquisition period, the growth rate was 59% in 2006 and 53% in 2007. it is believed that, if the wave of mergers and acquisitions had continued as experienced in 2004 and 2005, the positive spill-over effect would also continue in the sector.

4. Conclusion and Recommendations

4.1 Conclusion

This work is divided into four (4) sections, section one is the introductory part which provides the background to the study, the main objective of the study and the specific objectives. It is clear in the introduction that the work seeks to investigate the impact of merger and acquisition on economic growth. Attention is on experience in Nigeria, particularly, in the banking sector. The next section (section two) deals with the theoretical framework and conceptual issues. Theories and concepts in merger and acquisition, and the trend of mergers and acquisitions in Nigeria have been discussed.

Section three makes comparative analysis to show the effect of mergers and acquisitions on bank performance using total bank assets as proxy. The analysis has confirmed the theoretical a priori expectation that mergers and acquisitions impact positively on economic growth.

It is deduced from the analysis in section three (3) that growth rate of total bank assets used as proxy for bank performance was lower in the pre-merger and acquisition era as compared to the post era. However, the difference of 2% in average growth rate for the period reviewed was insignificant. This could be attributed to short period of active merger and acquisition in the sector. Mergers and acquisitions were mainly active in 2005. A significant impact was noticeable in 2006 at the growth rate of 59 percent. This was a spill-over effect of the high wave in 2005. Such experience of significant impact never occurred in the pre era of adoption of merger and acquisition in the banking sector.

4.2 Recommendations

Based on the findings, the following recommendations have been made:

i. It is recommended that merger and acquisition should be encouraged and adopted by government through the ministry of commerce and industry as a strategic plan to achieve both internal growth within industries and the Nigerian economy at large. The study has shown low wave of merger and acquisition in the real sector of the Nigerian economy, except in 2005 in the banking sector. Many industrialized economies had long embraced the concepts as process of structural adjustment and have achieved much economically.

ii. Many investors are ignorant of benefits of merger and acquisition. It is recommended that Ministry of Commerce and Industry should flag enlightenment campaign in the real sector of the Nigerian economy to educate, particularly investors on gains of merger and acquisition of firms.

iii. Also it is noticeable that after the high wave of mergers and acquisition in the banking sector in 2005, there still exist many weak banks in Nigeria. It is recommended that the process should be a continuous exercise to eliminate the weak banks and form stronger ones until at most 5 mega banks come to stay.

iv. As small and medium scale enterprises are welcomed in the Nigerian Stock Exchange, it is recommended that regulators of the stock exchange should make it a condition that 5-10 small and medium scale businesses should integrate horizontally, vertically or form conglomerate to enable them register in the market.

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TABLE 1: Trend of Mergers and Acquisition Real Sector of the Nigerian Economy

S/N	Year	The Companies
1	1983	A. V. Leventis and Co. Ltd. and Leventis Stores Ltd.
2.	1984	Lever Brothers Nig Ltd and Lipton Nigeria Ltd.
3.	1988	Lever Brother of Nig Ltd And Chesebrough Product Ltd.
4.	1989	Smithkline and Beecham (Smthkline Beecham)
5.	1995	Glaxo and Welcome (Glaxowelcome)
6.	1995	Unilever Nig. Ltd and Lever Brothers Nig Ltd.
7.	1995	Ciba-Geigy and Sandos (Norvatis)
8.	1995	Sona Breweries Nig. Plc and International Beer and Beverages Industries of Nigeria Ltd.
9.	1996	Nigerian Bottling Company Plc and Sapanda Industries Ltd.
10.	1996	PZ Industries Plc and Thermocool Nig Ltd.
11.	1996	Smithline Beecham Plc and Sterling Products Plc.
12.	1996	Nestle Foods Nig Plc and Nestle Nigeria Ltd.

Compiled from Sources: Akinsulire, 2008:568
www.Norvatis.com/about-norvatis/company-history/index.shtml-cached-similar.
www.nndbcom/company/667/000119312/-cached
http://www.globalbusinessinsights.com/content/rbfs0063m.pdf

TABLE 2: Component Members of Consolidated Banks

S/N	NAME	MEMBER OF THE GROUP
1	ACCESS BANK PLC	Marina bank, Capital Bank Int'l, Access Bank
2.	AFRIBANK PLC	Afribank Plc, Afribank International Ltd (Merchant Bankers)
3.	DIAMOND BANK PLC	Diamond Bank, Lion Bank, African International Bank (AIB)
4.	ETB PLC	Equatorial Trust Bank (ETB) Devcom
5.	FCMB PLC	FCMB, Co-operative Development Bank, Nigeria African Bank, Midas Bank
6.	FIDELITY BANK PLC	Fidelity Bank, FBS, Manny Bank
7.	FIRST BANK PLC	FBN Plc, FBN Merchant Bank MBC
8.	FIRST INLAND BANK PLC	IMB, Inland Bank, First Atlantic Bank NUB
9.	IBTC – CHARTERED BANK PLC	Regent, Chartered IBTC
10.	INTERCONTINENTAL BANK PLC	Global, Equity, Gateway, Intercontinental
11.	OCEANIC BANK PLC	Oceanic Bank Int'l Trust Bank
12.	PLATINUM - HABIB BANK PLC	Platinum Bank, Habib Bank
13.	SKYE BANK PLC	Prudent Bank, Bond Bank, Coop Bank, Reliance Bank ETB
14.	SPRING BANK PLC	Guardian Express Bank, Citizen Bank, Fountain Trust Bank, Omega Bank, Trans-International Bank, ACB
15.	STERLING BANK PLC	Magnum Trust Bank, NBM Bank, NAL Bank, INMB, Trust Bank of Africa
16.	UBA PLC	STB, UBA, CTB
17.	UNION BANK PLC	Union Bank, Union Merchant Bank, Universal Trust Bank, Broad Bank
18.	UNITY BANK PLC	New Africa Bank, Tropical Commercial Bank, Central – Point Bank, Bank of the North, NNB, First Interstate Bank, Intercity Bank, Societe Bancaire, Pacific Bank
19.	WEMA BANK PLC	Wema Bank, National Bank

Source: Union Digest Vol. 9 Nos. 3 and 4, December 2005 p.44/ Acha (2006)

TABLE 3A: Total Asset of Banks Prior to Adoption of Merger and Acquisition in the Banking Sector

Year	Total Asset of Banks (₦' Million)	Growth Rate (%)
1997	694,925.4	-
1998	821,233.6	18
1999	1,195,924.1	46
2000	1,707,103.5	43
2001	2,247,039.9	32
2002	2,766,880.3	24
2003	3,047,856.3	11

Source: CBN Statistical Bulletin 2010

Note: Merchant banks and Commercial banks figures were merged

TABLE 3B: Total Asset of Banks after Adoption of Merger and Acquisition

Year	Total Asset of Banks (₦' Million)	Growth Rate (%)
2004	3,753,277.8	-
2005	4,515,117.6	20
2006	7,172,932.1	59
2007	10,981,693.6	53
2008	15,919,559.8	45
2009	17,522,858.2	10
2010	17,331,559.0	-1

Source: CBN Statistical Bulletin 2010