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Mergers and Acquisitions in the Nigerian Banking Industry: An Explorative Investigation

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Abstract: The study was designed to examine mergers and acquisitions in the banking industry in Nigeria. The need to carry out this study arose from the challenges faced by Nigerian banks despite the reduction of banks from 89-25 at the end of 31st December 2005. These current challenges faced by banks in the country have made researchers to question the efficacy of the consolidation of banks in Nigeria. The explorative research method was used for this study. Data was collected from journals, textbooks, conference papers and the internet. The findings reveal that the consolidation (mergers and acquisitions) activities in Nigeria did not meet the desired objectives of liquidity, capital adequacy and corporate governance which have resulted to more troubled banks after the consolidation. On the basis of these, the study recommends among others that corruption, fraud and insiders abuses must be minimized in the banking industry for the country to derive the benefits of mergers and acquisitions of banks.

Key words: Acquisition, banks, banking industry, mergers, Nigeria, West Africa

INTRODUCTION

The banking industry in Nigeria plays a very significant role in the economic development of the country. According to Nzotta (2004), banks as part of the Nigerian financial system channel scarce resources from surplus economic units to deficit units and they exert a lot of influence on the pattern and trend of economic development through their lending and deposit mobilization activities.

This is why Abdullahi (2002) says the banking industry in particular play crucial role in the economic development by mobilizing savings and channeling them for investment especially in the real sector which increases the quantum of goods and services produced in the economy, thus national output increases and the level of employment improves. The banking industry in Nigeria is able to play the positive role only if it is functioning efficiently. However if it is repressed, inefficient and incapable of providing timely and quality services, the banking system could become a major hindrance to economic growth and development.

This led to dwindling confidence in the banking industry by Nigerians (Sanni, 2009). Adewoyin (2006) noted that bank failure has been experienced since 1990's during which period one out of every two banks was distressed and in the early 2000's when one out of every three banks was marginally unsound or totally unsound (Sanni, 2009). Soludo (2004) enumerated the fundamental problems of Nigerian banks, particularly those classified as unsound which include persistent illiquidity, poor assets quality and unprofitable operations and stated the major problems as follows: over-dependence on public sector deposits and neglect of small and medium class savers; weak capital base; insolvency as evidenced by negative capital adequacy ratios and shareholders' funds that had been completely eroded by operating losses; gross insider abuses, resulting in huge non-performing insider related credits; weak corporate governance and risk management practices.

The failure of banks in the 1990's and early 2000's made the former governor of Central Bank of Nigeria, Professor Charles Soludo to announce on July 6, 2004 that the minimum capital requirement base of banks in the country would be raised from #2 to #25 billion. The new policy which required banks to comply with the directive by end of December 2005 was aimed at significantly strengthening the operating environment of banks to perform their intermediation role effectively and efficiently. The new capitalization level for banks was to foster consolidation of the banking industry through mergers and acquisitions (M and A). Nzotta (2004)

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maintain that banks in Nigeria explored the option of mergers and acquisitions in an attempt to meet the capital base of #25 billion. Alao (2010) argue that Nigerian banks adopted different strategies to achieve the stipulated minimum capital base of #25 billion during the consolidation of banks in 2004 and 2005 which include mergers and acquisitions.

He further opines that mergers and acquisitions represents the most widely used corporate strategy to penetrate into new markets and new geographic regions, gain management expertise and knowledge or allocate capital. The question why mergers and acquisitions occur has multiple answers.

The often discussed reasons are synergy, agency costs due to self-serving acquirer managers, discipline of target management and managerial timing of high market valuation (Angwin, 2001; Rhodes-Kropf and Viswanathan, 2004; Shleifer and Vishny, 2003; Ayadi and Pujals, 2005; Higgins, 2009). However, Andrade *et al*. (2001) explain these reasons only weakly why mergers tend to occur in waves. According to Boot (2003), first-mover advantages and strategic advantages of market power and associated deep pockets may explain the current mergers and acquisitions wave and the broad scope of many of the players in the industry. Kaur and Kaur (2010) also noted that mergers and acquisitions in the banking industry are aimed at achieving economies of scale and scope. This is because as the size increases the efficiency of the system also increases. Mergers also help in the diversifications of products which help to reduce risk as well (Pilloff and Santomero, 1996). The economic rationale of mergers and acquisitions is based on the belief that the advantages can be obtained through the reduction of expenses and earning volatility and the increase of the market power and economic of scale and scope (Kiymaz, 2004).

Pilloff and Santomero (1996) argue that mergers and acquisition activities can significantly reduce operating costs from the fact that larger firms can be more efficient if redundant facilities are eliminated. On the other hand, DeYoung *et al*. (2009) argues that mergers and acquisitions can increase firm size. Firms with large size can increase market power in determining higher prices or generating profits.

Mergers and acquisition activities have drawn much attention in academic research. One stream of research investigates whether mergers and acquisitions can create or destroy value of shareholders and prior studies apply event study methodology to examine the market reaction around bank merger and acquisition (Cybo-Ottone and Murgia, 2000; Cornett *et al*., 2003; Croson *et al*., 2004; Ismail and Davidson, 2005). The litereature on the value of bank mergers and acquisitions presents a clear paradox. Empirical evidence indicates that on average, there is no statistical significant gain in value or performance from merger activity. Yet, mergers continue (Heid and Behr, 2008). However, some banks in Nigeria are still facing some of the problems that led to the 2004 and 2005 banks consolidation through mergers and acquisitions from a capital base of #2 to #25 billion. Therefore, the objective of this study is to critically analyse the mergers and acquisitions in the Nigerian Banking industry and offer some required therapy to ensure optimal success in mergers and acquisitions.

Theoretical framework and empirical studies

Nature and scope of mergers and acquisitions: The term merger refers to the combination of two or more organizations into one larger organization. Such actions are commonly voluntary and often result in a new organizational name (often combining the names of the original organizations). An acquisition, on the other hand is the purchase of one organization by another. Such actions can be hostile or friendly and the acquirer maintains control over the acquired firm (Jimmy, 2008; Alao, 2010). In the same vein, Gaughan (2007) defines merger as a combination of two or more corporations in which only one corporation survives. He further stated that the acquiring company assumes the assets and liabilities of the merged firm. Also, Sudarsanam (2003) stated that terms such as merger, acquisition, buyout and take over are used interchangeably and are all part of the merger and acquisition parlance but was quick to point out the differences when he described merger as the process whereby corporations come together to combine and share their resources to achieve common objectives with the shareholders of the merged firms still retaining part of their ownership and this may sometimes lead in new entity being formed while acquisition resembles more of an arm's length transaction with one firm purchasing the assets of the other and the shareholders of the acquired firm ceasing to be owners of the new firm.

Literatures on mergers and acquisitions, consistently discussed different types of mergers. These are horizontal, vertical, conglomerate and concentric mergers (Okonkwo, 2004; Gaughan, 2007). Vertical merger is a merger in which one firm supplies its products to the other. A vertical merger results in the consolidation of firms that have actual or potential buyer-seller relationships (Gaughan, 2007). A conglomerate merger occurs when unrelated organizations combine or firms which compete in different products markets which are situated at different production stages of the same or similar products combine to enter into different activity

fields in the shortest possible time span and reduce financial risks by portfolio diversification (Okonkwo, 2004; Gaughan, 2007). Concentric mergers and acquisitions involve firms which have different business operation patterns though divergent but may be highly related in production and distribution technology (Jimmy, 2008; Alao, 2010). A horizontal merger is the merger of two or more companies operating in the same field and in the same stages of process of attaining the same commodity or service.

Sudarsanam (2003) provide a five-stage model that will result in successful pursuit of synergistic gains from mergers and acquisitions. These stages are: corporate strategy development; organizing for acquisitions; deal structuring and negotiation; post-acquisition integration and post-acquisition audit and organizational learning. The corporate strategy development is concerned with ways of optimizing the portfolio of businesses that a firm currently owns and how this portfolio can be changed to serve the interests of the corporation's stakeholders. According to Lockett *et al*. (2009), the effectiveness of mergers and acquisitions in achieving corporate strategic objectives depends on the conceptual and empirical validity of the models. Organising for acquisition is a stage where firms lay down the criteria for potential acquisitions consistent with the strategic objectives and value creation logic of the firm's corporate strategy and business model.

Sudarsanam (2003) argues that an understanding of acquisition decision process is important, since it has bearing on the quality of acquisition decision and its value creation logic. The deal structuring and negotiation stage of mergers and acquisition is tricky business and it can have serious financial implications for both the acquirer and the acquired that does not possess the necessary experience or professional guidance due to asymmetric information (Angwin, 2001).

The post-acquisition integration involves the combination of distinct organizations into one, resulting in changes in both the target and the acquirer, to deliver the strategic and value expectations that informed the merger (Sudarsanam, 2003). The post-acquisition audit and organizational learning stage involves long-term plan evaluation, adjustment and capitalizing on success of mergers and acquisitions. Ghosh (2001) and Sudarsanam (2003) argues that specific performance measures such as financial measures as well as information system integration may be assessed for further development of capabilities and learning.

Motives of mergers and acquisitions: In theory, three motives of mergers and acquisitions have been documented in existing literature. These motives include the synergy motive, the hubris motive and agency motive. Each motive has its own implication in association with the benefits to the participant of the organizations in mergers and acquisitions. The synergy hypothesis has been widely documented in the existing literature in an attempt to explain the motive of mergers and acquisitions (Becher, 2000; Lensink and Maslennikova, 2008; Carline *et al*., 2009). This motive suggests that mergers and acquisitions occur when the combination of the two organizations results in economic gains. The Hubris hypothesis of mergers and acquisitions suggest that managers may overpay to targets as a result of valuation errors (Becher, 2000; Lensink and Maslennikova, 2008). Lensink and Maslennikova (2008) argue that the acquirer mistakenly believes that the value of the target is higher than its actual market value. As a result, the bidder overpays and realises negative gains while shareholders of the target profit. The agency hypothesis to account for motives of mergers and acquisitions argues that managers pursue their own interests to engage in takeover activity at the expense of shareholders (Lensink and Maslennikova, 2008).

Carline *et al*. (2009) also argue that managers may aim to their own interests by increasing firm size. Managers may also increase perquisite consumption that may damage firm value.

Mergers and acquisitions research paradigms: There are different study of mergers and acquisitions. Several researchers have given different perspectives of mergers and acquisitions. These mergers and acquisitions paradigms include: economic and finance; strategy; organizational behaviour and human resource management perspectives (Denis and McConnel, 2003; Flanagan and O'Shaughnessy, 2003; Ramaswamy and Waegelein, 2003; Marks and Mirvin, 2001; Buono, 2003; Millward and Kyriakidou, 2004).

The economic and finance paradigm is primarily interested in the efficiency impact of mergers and acquisitions on the economy through economies of scale and market power with emphasis on market for corporate control. One of the key arguments of the market for corporate control paradigm is that economic value created through acquisition activities is decided by market characteristics including its competitiveness (Denis and McConnel, 2003). Researchers using the strategy paradigm see mergers and acquisitions as a means of corporate growth and diversification, primarily emphasizing factors that are management controlled such as diversification strategies as a crucial factor in determining post-acquisition performance (Marks and Mirvin, 2001). Organizational behaviour researchers are interested in post integration process emphasizing both cultural clash and conflict resolution (Buono, 2003). The primary interests in human resource management

Table 1: Bank mergers and acquisitions in Nigeria between 2004 and 2005

New banks	Constituent members
Access Bank Nigeria Plc	Access Bank, Marina Int'l Bank and Capital Bank International
Afribank Nigeria Plc	Afribank Plc and Afribank Int'l (Merchant Bankers)
Bank PHB Plc	Platinum Bank Limited and Habib Nigeria Bank Limited
Diamond Bank Plc	Diamond Bank, Lion Bank and African International Bank
Equatorial Trust Bank Plc	Equatorial Trust Bank Ltd. and Devcom Bank Ltd.
Fidelity Bank Plc	Fidelity Bank, FSB International Bank and Manny Bank
First Bank of Nigeria Plc	First Bank Plc, MBC International Bank and FSB (Merchant Bankers)
First City Monument Bank Plc	First City Monument Bank, Coop Development Bank, Nigeria-American Bank and Midas Bank
First Inland Bank Plc	First Atlantic Bank, Inland Bank (Nigeria) Plc, IMB International Bank Plc and NUB International Bank Plc
IBTC-Chartered Bank Plc	IBTC, Chartered Bank Plc and Regent Bank Plc
Intercontinental Bank Plc	International Bank Plc, Global Bank Plc, Equity Bank of Nigeria Limited and Gateway Bank of Nigeria Plc
Oceanic Bank International Plc	Oceanic Bank International Plc and International Trust Bank
Skye Bank Plc	Prudent Bank Plc, Bond Bank Limited, Reliance Bank Limited, Cooperative Bank Plc and EIB International Bank Limited
Spring Bank Plc	Citizens International Bank, ACB International Bank, Guardian Express Bank, Omega Bank, Trans International Bank and Fountain Trust Bank
Sterling Bank Plc	Trust Bank of Africa Limited, NBM Bank Limited, Magnum Trust Bank, NAL Bank Plc and Indo-Nigeria Bank
United Bank for Africa Plc	United Bank for Africa Plc, Standard Trust Bank Plc and Continental Trust Bank
Union Bank of Nigeria Plc	Union Bank of Nigeria Plc, Union Merchant Bank Ltd., Broad Bank of Nigeria Ltd. and Universal Trust Bank Nigeria Plc
Unity Bank Plc	Intercity Bank Plc, First Interstate Bank Plc, Tropical Commercial Bank Plc, Centre-point Bank Plc, Bank of the North, New African Bank, Societe Bancaire, Pacific Bank and New Nigeria Bank
Wema Bank Plc	Wema Bank Plc and National Bank of Nigeria Ltd.

Central Bank of Nigeria (2005)

perspective are the psychological effects of mergers and acquisitions on individuals such as feelings of tension, alienation and uncertainty. The organizational behaviour and human resource perspectives indicate that it is basically the problem that contributes to the success and failure of mergers and acquisitions (Marks and Mirvin, 2001; Ford and Harding, 2003; Sudarsanam, 2003).

Evolution of the Nigerian banking industry: Banking in Nigeria went through phases and covers a wide span of time from an era of free banking or virtually absolute freedom in tune with the dictate of the economies of classical liberalism, to the era of rigid or strict potential regulations. According to Jimmy (2008) and Alao (2010), the history of banking in Nigeria is divided into four phases: the embryonic; expansion; consolidation/reform and post-consolidation phases. The embryonic phase of banking evolution dates back to 1892 when the African Banking Corporation of South Africa, established a branch in Lagos followed by the British Bank of West Africa in 1894 while Barclays Bank DCO (Dominion, Colonial and Overseas) and the British and French Bank for commerce and industry were established in 1925 and 1949, respectively.

Indigenous banking in Nigeria started with the establishment of National Bank of Nigeria Limited in 1933, Agbonmagbe Bank Limited in 1945 and the African development Bank Limited in 1948. The expansion phase of banking evolution was the establishment of Rural Banking Scheme in 1977, Peoples' Bank in 1989 and community Banks in 1990. The consolidation phase started with the 2004 and 2005 mergers and acquisitions of banks where 89 banks were reduced to 25. The post-consolidation phase is the clamouring and calling for mega banks in the country through Foreign Bank penetration from the United States and Europe, respectively. Nzotta (2004) noted that the evolution of modern banking in Nigeria can be classified into nine different phases as shown below.

Table 2: Evolution of banking in Nigeria

Phases	Date	Period
First	Upto1952	Free banking era
Second	1952-1959	Pre-central banking era
Third	1959-1970	Era of banking legislation
Fourth	1970-1976	Era of indigenization
Fifth	1977-1985	Post okigbo era
Sixth	1986-1992	De-regulation era
Seventh	1993-2001	Era of bank distress
Eighth	2002-2004	Universal banking era
Nineth	2004-Date	Era of bank consolidation

Nzotta (2004)

Mergers and acquisitions' activities in the Nigerian Banking industry: The Nigerian Banking industry has gone through a lot of transformations as regards mergers and acquisitions. Prior to the mergers and acquisitions wave of 2004 and 2005, the acquisition of African Banking Corporation in 1894 by The British Bank for West African (now First Bank of Nigeria Plc) and Union Bank of Nigeria's acquisition of Citi Trust Merchant Bank for #167.75 million in 1995 were the major bank merger and acquisitions in Nigeria (Table 1). Between July 6, 2004 and December 31, 2005, the number of banks in Nigeria reduced from 89-25 courtesy of mergers and acquisitions and forced withdrawal of banking license from institutions that were unable to achieve the new paid-up capital of #25 billion. Out of the tweny five banks that achieved the #25 billion requirements, Table 2 showed that fourteen of them were the product of mergers and acquisitions involving sixty nine banks while only six grew organically (Central Bank of Nigeria, 2005). The wave

Table 3: Empirical Studies of mergers and acquisitions

Researchers	Samples and Methods	Main results
Kaur and Kaur (2010)	The study used time-series cross section data of commercial banks in India for the period, 1990-1991 to 2007-2008 using non-parametric data envelopment analysis technique	The findings of the study suggest that over the entire study period average cost efficiency of public sector banks found to be 73.4 and for private banks is 76.3%. The findings suggest that merger programme has been successful in Indian banking industry
Altunbas and Ibanez (2004)	A sample of 262 completed deals of which 207 were domestic and 55 cross-border mergers in the European Union banking sector between 1992 and 2001. Using descriptive statistics, regression and correlation analysis for the purpose of data analysis	The study showed that on average, bank mergers in the European Union resulted in improved return on capital. The study also found significant difference between domestic and cross border mergers
Fuentes and Sastre (1998)	Using panel data for Spanish banks from 1988-1997 using financial ratios, Wald test, Sargan test and auto correlation test or data analysis	The study shows some insights during the pre and post-merger periods of the effects of mergers and acquisitions on efficiency, profitability and strength of consolidated institutions
Da Silva and Diz (2005)	A sample of banks in the Portuguese banking industry from 1995-2003 using Patell and Boehmer tests	The study shows some targets gains but no gains for the bidders
Jimmy (2008)	A sample of two banks (Access Bank and Zenith Bank) using financial ratios and exploratory research	The result suggests that Access Bank that pursued mergers and acquisitions witnessed a faster growth rate and Zenith Bank that pursued organic growth was able to sustain its quality performance trends
Altunbas and Marques	Descriptive statistics and regression analysis for the purpose of data collection	The study showed that on average, bank mergers have resulted in improved performance
Heid and Behr (2008)	A sample of 474 mergers for the period, 1995-2000 and descriptive statistics for the purpose of data analysis	The result shows that there is a neutral effect of mergers on profitability and a positive effect on cost efficiency

of mergers and acquisitions that began 2004 has not abated as the merger between IBTC Chartered Bank Plc and Stanbic Bank of Nigeria Limited after the December 31, 2005 deadline has further reduced the number of banks from 25-24 while those banks that were unable to recapitalize which were earmarked for liquidation by the banking regulatory authorities have virtually been acquired by successfully recapitalized banks.

Empirical literature: Empirical studies have explained the importance of mergers and acquisitions (Andrade *et al.*, 2001; Shleifer and Vishny, 2003; Rhodes-Kropf and Viswanathan, 2004). Table 3 shows a summary of sample, methodology and main results of these studies.

MATERIALS AND METHODS

The study used exploratory research to investigate the mergers and acquisitions in the Nigerian Banking industry. The study relied primarily on secondary data from academic journals, text books, companies' annual reports and internet sources and the analysis was mainly descriptive.

RESULTS AND DISCUSSION

The driving force in bank mergers and acquisitions include better risk control through the creation of critical mass and economies of scale, advancement of marketing and product initiatives, improvements in overall credit risk and technological exploitation. These drivers have led to improved operational efficiencies and larger and capitalized institutions. The results of this policy are neither here nor there contrary to the policy expectations. The most difficult aspect of consolidation is the ones induced by government through mergers and acquisitions (Somoye, 2008).

This led to dramatic growth in the Nigerian banking industry. Sanusi (2010) however says neither the industry nor the regulators were sufficiently prepared to sustain and monitor the sectors explosive growth. Prevailing sentiments and economic orthodox all encouraged this rapid growth, creating a blind spot to risk building in the system. Table 4 and 5 shows the state of Nigerian banks. Table 4 shows that out of the twenty five banks that merged, ten were classified as sound, five satisfactory, five marginal and five unsound. This implies that the mergers and acquisitions done in 2005 by Nigerian banks did not solve the problems of banks in the country. Somoye (2008) opine that the reason that may be advanced for the present state of Nigerian Banks after the 2005 mergers and acquisitions could be viewed from the perspective of wrong planning. Shih (2003) points out the possibility that credit risk could increase in the event of a sound bank merging with an unsound bank.

Salleo in Somoye (2008) added that if a voluntary consolidation does not enhance the performance of the participating banks, any performance enhancing effect of the consolidation promoted by the government policy is more questionable. Table 5 shows the ten troubled banks based on Central Bank of Nigeria, audit of banks based on the three criteria of liquidity, capital adequacy and corporate governance. Wema Bank Plc was asked to recapitalize and Unity Bank Plc performed well in liquidity

Table 4: State of Nigerian banks after consolidation

Categories	2005	2006
Sound	25	10
Satisfactory	-	5
Marginal	-	5
Unsound	-	5

CBN publication (2006)

Table 5: Troubled banks after 2005 mergers and acquisitions

Name of banks	Capital after merger and acquisitions (end of 2006)
Union Bank Plc	#95.70^{b}
Intercontinental Bank Plc	53.90^{b}
Wema Bank Plc	31.90^{b}
Unity Bank Plc	30.00^{b}
Bank PHB Plc	28.50^{b}
Oceanic Bank International Plc	37.70^{b}
Afribank Nigeria Plc	24.90^{b}
Spring Bank Plc	25.00^{b}
Finbank Nigeria Plc	25.40^{b}
Equitorial Trust Bank Ltd.	28.40^{b}

CBN reports

and corporate governance but had problem with capital adequacy. But the remaining eight banks failed in the three criteria. However, as developments within the Nigerian banking industry reveals banks in the country are still facing those challenges that led to the 2005 mergers and acquisitions.

These challenges include: service delivery is still patchy, infrastructure is still weak and regulation and reporting, though improving, remains wanting, skill gap and a lack of professionalism, over reliance on cheap public sector fund, corporate governance remains inconsistent, weak credit assessment skills, liquidity issues and capital issues, etc. According to CBN eight banks had government equity holding above 10%; three banks had two or more members of their families on the board; no bank had complied with the requirement for independent directors and seven banks had executive directors as members of their board audit committees contrary to the provisions of the code of corporate governance for Banks in Nigeria. For some of the banks, the mergers and acquisitions were so complex that even today, it cannot be said to be satisfactorily completed.

CONCLUSION

The aim of this study was to examine the mergers and acquisitions in the Nigerian banking industry. The researchers utilized a relatively simple and parsimonious approach following mergers and acquisitions in 2005 that left the country with twenty four banks. However, despite the mergers and acquisitions of banks in the country, some of the merged banks are still facing those challenges that led to the 2005 consolidation. These challenges include; poor risk management, poor corporate governance practices, over reliance on public sector funds, weak infrastructure, insufficient regulation and reporting, weak credit assessment skills, lack of professionalism and skills gap, etc. On the basis of the findings, the study made the following recommendations: to improve risk management culture, particularly in developing strong asset quality measures; banks need to develop more long-term funding which will help them in funding more long term projects. The issue of corruption, fraud and insider abuses needs to be minimized in the Nigerian banking industry for banks in the country to benefit from mergers and acquisitions, government and policy makers should be more careful in promoting mergers and acquisitions as a way of achieving capital adequacy, liquidity and good banking practices in Nigeria.

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