

Effect of Merger and Acquisition Practice in Financial Institutions of Nepal

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Abstract

The merger and acquisition serve as a disciplinary device for the bank management to improve the performance of the bank or as a means of implementing unpleasant business measure. This study aims to study the effect of merger and acquisition practice based on perceptions of personnel of financial institutions of Nepal. For the study, a closed-end questionnaire has been prepared and distributed among 180 banking personnel of three merged commercial banks (i.e. NIC Bank Ltd. and Bank of Asia Ltd., Global IME Bank Ltd. and Commerce & Trust Bank Ltd., and Prabhu Bank Ltd. and Grand Bank Nepal Ltd.) to analyze their views towards banking merger process. Out of them 80 (53.33%) questionnaires have been returned and used in this study. The results of this study indicate that merger and acquisition affect the liquidity position of the bank. The results also show that M&A practices increase the capital base of BFIs & thus develop the competent capabilities.

Keywords: Merger, Acquisition, Commercial banks, Development banks, Finance companies, Nepal Rastra Bank

Introduction

Mergers and acquisitions (M&A) is commonly used business strategy by companies to strengthen and maintain their position in market place. It is considered as a relatively fast and efficient way to expand into new markets and incorporate new technologies. It has become a key part of many corporate business strategies. M&A is a very important strategy for companies which want to expand their market share or size (Fairfield-Sonn, Ogilvie, & DelVecchio, 2002).

There are many reasons as to why banks and financial institutions (BFIs) engage in merger and acquisition practices. The merger in context of bank is initiated for varied reasons such as for cost cutting through economies of scale, gaining access to a new market, strengthening a company's marketing position, global expansion, gaining a talented work force, acquiring new knowledge and expertise, gaining a new computer base and pursuing new technologies. Such M&A enables BFIs to take benefit from new business opportunities that have been created by changes in the regulatory and technological environment. It also helps for improvement in cost and profit efficiency. It also leads banks to earn higher profits through the banks market in leveraging loans and deposit interest rates (Sufian, 2004). The merger and acquisition may therefore serve as a disciplinary device for the bank management to improve the performance of the bank or as a means of implementing unpleasant business measure.

Even though it has more than 120 years long history internationally, BFIs adopted merger strategy very lately in Nepal. When Nepal Rastra Bank (NRB) adopted the liberal licensing policy as the consequence there was a tremendous growth in numbers of BFIs. Now the overcrowding is hurting the financial sector of Nepal. NRB is a supervisory and regulatory body of all the BFIs in Nepal. Shrestha (2012) stated that when this bank has issued merger by-laws in May 2011, the concept of M&A was an entirely new thing to the BFIs of Nepal. The objective of the merger by-laws was to strengthen the BFIs position and performance by reducing the number of institutions. The merger bylaws have a provision that pressurizes all BFIs to go for an immediate merger in the form of consolidation. Lack of specific Act and provisions regarding acquisitions and geo-political scenario are major challenges.

After accession to the WTO in 2004 the NRB, the central bank of Nepal, has unveiled the policies to establish foreign bank branches in the country. To face the giant and big banks' challenges, bank should be big and efficient which is possible only through the means of M&A. Merger and acquisition of Nepalese banks and financial institutions is also necessary for the capacity building of these institutions to invest in the mega projects that helps for the formation of

the infrastructure. Realizing the situation of banking industry of the country, NRB has also issued “Merger Bylaws 2068” in 2011 which facilitates the M&A of BFIs. Further, central bank is also working on the forced merger policy for the financial institutions of the same group. NRB is prioritizing M&A of Nepalese BFIs to halve the number of BFIs in the country as per the recommendation of International Monetary Fund (IMF) which has assured NRB to help with budgetary assistance to manage the financial institutions of Nepal.

Very little research is carried out to know whether or not the merger by laws, acts and provisions regarding merger and acquisition issued by NRB is effective enough to correct the recent banking and financial turmoil such as low volume of turnover, high interest rate in lending, high interest rate spread, inefficient management, lack of project financing practice, inadequate working fund and unhealthy competition among BFIs. Thus, this study tries to explore whether merger and acquisition practices affect on liquidity position, performance, capital base to develop competent capabilities, financial capability and competitiveness of BFIs or not. It also tries to observe whether M&A requires liberal and well defined corporate law and financial discipline and transparency and accountability in corporate governance of BFIs or not. It further observes whether merger process in Nepal has supported the objective of financial stability or not.

Research Hypotheses

The research hypotheses of this study are as follows:

- H 1:** M&A affect the liquidity position of the bank.
- H 2:** M&A has positive impact on performance of banking institution.
- H 3:** M&A increase the capital base of BFIs & thus develop the competent capabilities.
- H 4:** M&A promote financial capability and competitiveness through shared skills.
- H 5:** Development of market for M&A requires liberal and well defined corporate law and financial discipline.
- H 6:** Development of market for M&A requires transparency and accountability in corporate governance.
- H 7:** M&A process in Nepal has supported in reducing the number of BFIs but the objective of financial stability has not been achieved.

Research Methods

In this research, descriptive and inferential analyses are used. For the study the primary data are collected through questionnaire. For the study, a closed-end questionnaire has been prepared and distributed among 180 banking personnel of three merged commercial banks (i.e. NIC Bank Ltd. and Bank of Asia Ltd., Global IME Bank Ltd. and Commerce & Trust Bank Ltd., and Prabhu Bank Ltd. and Grand Bank Nepal Ltd.) to analyze their views towards banking merger process. Out of them 80 (53.33%) questionnaires have been returned and used in this study. The respondents are divided as staff of commercial banks, development banks and finance companies in equal proportion. The respondents are first clarified about the objectives of the study and then enlightened them on filling the questionnaire. The data so obtained from them are then coded, tabulated and finally interpreted. Table 1 shows the demographic characteristics of respondents.

Table 1: Demographic Characteristics of Respondents

	Frequency	Percent
Type of Organization		
Commercial Bank	45	56.25
Development Bank	23	28.75
Finance Company	12	15
Gender		
Male	33	41.25
Female	47	58.75
Age		
20-30	43	53.75
31-40	28	35
41-50	9	11.25

Qualification		
Bachelor	46	57.5
Masters	34	42.5
Experience		
1-3 years	33	41.25
4-6 years	23	28.75
7-9 years	17	21.25
10 years and above	7	8.75
Post		
Officer	27	33.75
Senior Officer	12	15
Manager	4	5
Assistant	37	46.25

Data Analysis and Results

This section presents the data that were collected from the survey and their analysis for achieving results.

Descriptive Analysis

Descriptive analysis shows the results such as mean, standard deviation and alpha that are presented in the following table:

Table 2: Scale Mean, S.D and Cronbach's Alpha

Statements	Group	N	Mean	S.D.	Alpha
M&A affect the liquidity position of the bank	Commercial Bank	45	56.25	3.36	0.85
	Development Bank	23	28.75	2.87	
	Finance Company	12	15	2.58	
M&A has positive impact on performance of banking institution.	Commercial Bank	45	56.25	2.36	0.43
	Development Bank	23	28.75	2.61	
	Finance Company	12	15	2.25	
M&A increase the capital base of BFIs & thus develop the competent capabilities	Commercial Bank	45	56.25	3.24	0.21
	Development Bank	23	28.75	3.61	
	Finance Company	12	15	2.71	
M&A promote financial capability and competitiveness through shared skills	Commercial Bank	45	56.25	2.76	0.53
	Development Bank	23	28.75	2.78	
	Finance Company	12	15	3.00	
Development of market for M&As requires liberal and well defined corporate law and financial discipline.	Commercial Bank	45	56.25	2.51	0.17
	Development Bank	23	28.75	3.04	
	Finance Company	12	15	2.67	
Development of market for M&As require transparency and accountability in corporate governance	Commercial Bank	45	56.25	2.58	0.16
	Development Bank	23	28.75	3.26	
	Finance Company	12	15	3.08	
M&A process in Nepal has supported in reducing the number of BFIs, but the objective of financial stability has not been achieved.	Commercial Bank	45	56.25	3.18	0.49
	Development Bank	23	28.75	2.96	
	Finance Company	12	15	3.08	

The results show that out of total respondents the commercial banks personnel (mean = 3.36; S.D. = 0.17) are agreed that M&A affect the liquidity position of the bank. The personnel of development bank (mean = 2.61; S.D. = 0.53) are agreed that M&A has positive impact on performance of banking institution. Similarly the same personnel of

development bank are agreed (mean = 3.61; S.D. = 0.17) are agreed M&A increase the capital base of BFIs & thus develop the competent capabilities. Likewise, personnel of finance companies agreed (mean = 3.00; S.D. = 0.21) that M&A promote financial capability and competitiveness through shared skills.

Out of total respondents the personnel of development banks are also agreed (mean = 3.04; S.D. = 0.52) that development of market for M&As requires liberal and well defined corporate law and financial discipline.

They are also agreed (mean = 3.26; S.D. = 0.44) that development of market for M&As require transparency and accountability in corporate governance. Out of total respondents the commercial banks personnel (mean = 3.18; S.D. = 0.49) are agreed that M&A process in Nepal has supported in reducing the number of BFIs, but the objective of financial stability has not been achieved.

Hypotheses Testing

In this analysis, one way ANOVA test has been performed between the type of organization and the respondents' viewpoint to different statements of merger and acquisitions for testing study hypotheses.

Table 3: Hypotheses Testing

Statements	Group	N	F-value	P-value	Remarks
M&A affect the liquidity position of the bank	Commercial Bank	45	3.22	0.05	Significant
	Development Bank	23			
	Finance Company	12			
M&A has positive impact on performance of banking institution.	Commercial Bank	45	0.93	0.40	Insignificant
	Development Bank	23			
	Finance Company	12			
M&A increase the capital base of BFIs & thus develop the competent capabilities	Commercial Bank	45	3.69	0.03	Significant
	Development Bank	23			
	Finance Company	12			
M&A promote financial capability and competitiveness through shared skills	Commercial Bank	45	0.48	0.62	Insignificant
	Development Bank	23			
	Finance Company	12			
Development of market for M&As requires liberal and well defined corporate law and financial discipline.	Commercial Bank	45	2.54	0.09	Insignificant
	Development Bank	23			
	Finance Company	12			
Development of market for M&As require transparency and accountability in corporate governance	Commercial Bank	45	3.36	0.04	Significant
	Development Bank	23			
	Finance Company	12			
M&A process in Nepal has supported in reducing the number of BFIs, but the objective of financial stability has not been achieved.	Commercial Bank	45	0.46	0.64	Insignificant
	Development Bank	23			
	Finance Company	12			

The above table shows viewpoint of respondent working in commercial bank, development bank and finance company regarding the merger and acquisitions. Since P-value is less than 0.05, we can say that there is significant relationship between type of organization and following statements regarding merger and acquisitions. Therefore, the results supported the hypotheses H1, H3 and H6.

Since P-value is more than 0.05, we can say that there is no significant relationship between the type of organization and various statements regarding merger and acquisitions. Thus, the results did not support the hypotheses H 2, H 4, H 5 and H 7.

Findings and Conclusions

The results of this study indicate that merger and acquisition affect the liquidity position of the bank. The results also show that M&A practices increase the capital base of BFIs & thus develop the competent capabilities. Further,

the results also show that development of market for M&A requires transparency and accountability in corporate governance. However, the results show that M&A has no significant impact on performance of banking institution. Based on these results it can be concluded that there is no guarantee of merger practices that may not promote financial capability and competitiveness through shared skills. Further, it can be concluded that corporate law and financial discipline may not play major role for development of market in case of M&A practices. Even though merger process in Nepal has supported in reducing the number of BFIs but the objective of financial stability has not been achieved in the reality.

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Further Readings

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