THE EFFECTS OF MERGERS AND ACQUISITION ON CORPORATE GROWTH AND PROFITABILITY: EVIDENCE FROM NIGERIA

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ABSTRACT

It is a widely held view that a strategic solution to financial distress in corporate organizations is mergers and acquisitions. This view remains a presumption, which has not been empirically tested through a research study. Corporate organizations facing difficulty have in recent times often followed or are compelled by regulators to follow the path of extensive reconstruction through mergers and acquisitions, apparently as the only option to liquidation. This paper fills a gap in the literature by investigating the effects of mergers and acquisitions on the efficiency, growth and profitability of corporate organizations in the post consolidated environment of the Nigerian banking industry. The methodology used is a survey of companies incorporated in Nigeria under the Companies and Allied Matters Act [1990], which have undergone a merger or an acquisition process. The elements of the survey were selected randomly. A total of ten incorporated banks were selected using simple random sampling technique. The collected data were analyzed using key financial ratios. The results support the idea that mergers and acquisitions are not a prima facie solution to the problem of financial distress in corporate organizations. This is especially so when mergers are regulatory imposed than business environment driven. The study further revealed that while mergers and acquisitions can drive growth and profitability in some organizations, operating efficiency suffers at least in the short-term in the post merger and acquisition corporate entity. The evidence also shows that mergers and acquisitions provided only a temporary solution to financial distress and no solution at all to operating indiscipline.

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KEYWORD: Merger, Acquisition, Corporate Growth, Profitability**.**

INTRODUCTION

Business Organizations are established to achieve certain corporate objectives including corporate growth and increases in profitability. Growth is a major yardstick by which the success of a business firm is measured. Given that business organizations operate in a dynamic macroeconomic environment such growth is threatened in periods of volatile economic instabilities (Weston and Copeland, 1989). The resultant effect of the recent world economic meltdown is a financial crisis among corporate organizations. One strategy open to corporate organizations during the periods of economic crisis is Merger and Acquisition. Companies have been combining in various configurations since the early days of business. Nevertheless, joining two companies is a complex process because it involves every aspect of both companies. For instance, executives have to agree on how the combination will be financed and how power will be transferred and shared. Also the companies must deal with layoffs, transfers, changes in job titles and work assignments etc. (Staul, Mendenhall & Weber, 2005; Indhumathi, Selvam & Babu, 2011). The most popular forms of business combination are mergers, acquisition and consolidations.

Merger and acquisition is at its infancy stage in Nigeria compared with other developed countries. Merger and Acquisition is an important concept that contributes to the growth of a national economy through increase in productivity and profitability. Mandi (2003:3) contributing in this regard said that:

> "*In the last three years, growth through acquisition has been a critical part of the success of many companies operating in the new economy. In fact, I would say that merger and acquisition has been the single most important factor in building up their market capitalization*".

Merger has been defined as the combination of two or more separate firms into a single firm. The firm that results from the process could take any of the following identities: Acquirer identity or a complete new identity (Hitt, Harrison & Ireland, 2000). Mergers, Amalgamations and Takeovers have been identified as important features of corporate structural changes (Pandey, 2000).

The current economic situation in Nigeria can best be described as very turbulent with the problems reflecting more in the financial service sector. The dimension of the problem is such that banks in the country are fast losing their market share, in addition to facing continuous operating losses and liquidity crisis leading to inability to pay depositors. Other major challenges facing banks in the country include low turnover, low profit, low dividend payout, declining growth rate and high operating cost. The crisis in the financial sector reached a peak in July 2004 when the then Governor of Central Bank of Nigeria (CBN), Charles Soludo described the Nigerian Banks as 'fragile'. He disclosed that Nigerian Banks "as at the end of march 2004, the CBN's ratings classified 62 banks as sound/satisfactory, 14 as marginal and 11 as unsound while 2 of the banks did not render any return during the period". The Central Bank also reported that 45 banks or more than one-half of banks in operations recorded loan-deposit ratios of 100 per cent and above and 21 banks failed to meet the minimum liquidity ratio. A more fundamental restructuring policy was clearly needed for the banking industry (CBN, 2008).

The Central Bank Governor summarized the major problems facing the Nigerian Banking industry as weak corporate governance, evidenced by high turn over in the Board and management staff, inaccurate reporting, late or non-publication of annual accounts, gross insider abuse, insolvency, week capital base… Based on the foregoing problems, the Central Bank of Nigeria (CBN) came up with a major policy reform that required Banks licensed in Nigeria to increase their paid up capital to a minimum of N25 billion (Twenty five billion Naira) on or before 31st December 2005. These problems together with the CBN policy lead to serious financial crisis. It was alleged that the only solution available to these organizations to get out of the financial crisis is Merger and Acquisition.

The literature is rich with studies on Mergers and Acquisitions but very few of these studies, if any, focused on the effect of mergers and acquisitions on corporate growth, efficiency and profitability. This study fills this research gap by addressing the issue of whether merger and acquisition is the best solution to bail out an organization in financial crisis and the effects of merger and acquisition on corporate profitability. We using the sample survey method and draw secondary data collected from financial statements, reports and accounts. We examine 10 randomly selected banks form the existing recapitalized 25 banks. We evaluate the financial status of banks during pre and post mergers periods covering a sample period of 2004-2008 with the principal aim of determining the effect of merger on corporate growth and corporate profitability in Nigeria. Following the introductory section, the rest of the paper is structured as follows; Section II is the literature review while section III covers data and methodology. Section IV presents the result of the study while section V concludes the study.

LITERATURE REVIEW

This section reviews the relevant literature. The review also covers empirical studies in the area focusing attention on the research problems. It will also review the condition and legal framework upon which Merger and Acquisition is based in Nigeria.

David (1968) reveals that most countries have no good record of Merger and Acquisition development. However, it was on record that the first incidence occurred between 1890 and 1904 in the United State of America. The second incidence was in 1920 at the end of the First World War. The third incidence occurred at the latter part of the Second World War (between 1939 and 1945) during which large numbers of manufacturing and mining firms totaling about 2400 merged. Therefore, internationally, mergers and acquisitions constitute the most frequently used means through which firms undertake foreign direct investments. In most cases this has recorded a low level of success due to cultural due diligence, cross cultural communication, connection, and control (Rottig, 2007, Askim, Christensen, Fimreite and Laegreid, 2008). Also, Vaara, (2003) noticed that this could lead to lack of trust, reduced commitment and conflict. Similarly, it could be due to the fact that most negotiations focus more on financial or economic perspectives which are usually measured in the short-run, neglecting the unanticipated long-run returns and non-financial factors (Mansure, 2003; Iyoha & Adeyomo, 2007; Majidi, 2007, Gbede, 2008). While, Nehavandi and Malekzadeh (1998) made it clear that the level of success in merger and acquisition depend strongly on the level of congruence between both firms in the negotiation process and difficulties in the process could be ameliorated by post-acquisition integration negotiations.

In Nigeria, Merger and Acquisitions remain few and unpopular. The earliest known merger and acquisition that occurred in Nigeria was in 1926 between West African Soap Company Ltd and Van Der Berg Ltd (producers of margarine) Shamsudeen (1997). Since then there have been increased discussion and awareness on Merger and Acquisitions in Nigeria. The decade 1995 and 2005 was traumatic for banking industries in Nigeria which led to distress and in general, the overhauling of the industry. In 2004, the regulating body prescribed a minimum shareholders' fund of 25billion Naira for licensed Banks operating in Nigerian. This financial crisis led to Mergers, Acquisition or Consolidation in the industry. The result of this policy was that out of 89 banks that were then in operation, 75 representing 80% merged into 25 banks while the remaining 14 representing 20% that could not finalize the merging process went into liquidation. Table 1 shows successful mergers in Nigeria from 1982 to 1988. Table 2 shows successful merger in the banking industry in 2006. There are other successful mergers in Nigeria from 2006 to-date.

<u>Meaning of Mergers, Acquisitions and Consolidation</u>

The terminologies, 'Merger, Acquisition and Consolidation' often cause confusion in the minds of people. The difference between a merger and a consolidation is fairly technical having to do with how the financial and legal transaction is structured (Bovee and Thill, 2001). Basically, in a merger, one company buys another company, or parts of another company and assumes control of its property and liabilities. a Consolidation, is the combination of two or more companies in which the old companies cease to exist and a new enterprise is created while Acquisition is a form of business combination in which one company buys another company's voting stock (Healy, Palepu and Ruback, 1997).

Merger can be defined as "any amalgamation of the undertaking or any part of the undertakings or interest of two or more companies or the undertakings or part of the undertakings of one or more companies and one or more corporate bodies" (Company and Allied Matters Act (CAMA) 1990 : S.590). According to Coyle (2000), merger is the coming together of two companies of roughly equal size pooling their recourses into a single business.

Table 1: Successful Mergers in Nigeria from 1982 to 1988

Acquiring Company	Target Company	Year	Conversion Terms	Effects on Financing
1.A.G Leventis Nigeria Limited Public quoted	Leventis Stores Limited Public quoted	1983	A price of 60k per 50k share for A. G. Leventis and a price of 50k each for the shares of leventis Stores giving rise to an exchange ratio of 80 per cent i.e. 100 ordinary shares of Leventis stores for 83 ordinary shares of A.G. Leventis Ltd	A.G. Leventis had to increase its Authorized Capital to enable it issue 11,718, 750 ordinary shares in Exchange for 14,062,500 Ordinary
2. Lever Brothers Nigeria Limited Public quoted company	Lipton Nigeria Limited Private Company	1984	A price of 80k per 50k share for lever Brothers and N1.20 per 50k share for Lipton, giving rise to an exchange ratio of 150 for 100 i.e., 150 Ordinary shares of LBN for 100 ordinary shares of Lipton	LBN had to increase its Authorized Capital to enable it to issue 11,340,000 Ordinary shares in exchange for 7,560,000 Ordinary shares of
3. John Holt Limited Public quoted Company	Bauchi Bottling Company Limited. Private Company	1985	Payment of N5,185,000 to clear Bauchi Bottling's outstanding debts and N1,230,400 to pay off the share holders of the company in respect of their equity capital	Cash
4. SCOA Nigeria Limited. Public quoted Company	Nigerian Automotive Components Limited Private Company	1985	The entire shares of NIACO were offered for N1.00 and SCOA was to manage NIACO to ensure the remittance to FIMM of N500,000 as full and final settlement of the debt of N1,716,343 due from NIACO to FIMM	Cash
5. Intra Motors Nigeria Limited Public quoted	West Coast Fisheries Limited. Private Company	1985	A price of N1.50 per shares for West Coast Fisheries was approved. This put the total value of West Coast Fisheries at N150,000 and it was settled by cash	Cash
6. ITI Nigeria Limited Private Company	Henein Spinning Mills Ltd. Private Company	1985	A price of N6.50 per N2.00 share of Henein Mills Limited was approved for the entire 745,973 shares of N2.00 each acquired by ITI Limited	Cash
7. Niger Match Company Limited (Now Associated Match) Industries	a. United Match Company of Nigeria. b. Star Match	1985	A par price of N1.00 per share for United match Company, Star Match Company, and Safa Splints Limited was approved by the NSEC Exchange of Shares	There was no monetary consideration as regards Kaduna Match Limited as it had not issued its initial capital and its existing assets were
8. SCOA Nigeria Limited Public quoted Company	Motor Services Engineering Ltd. (MOSEL) Private Company	1986	A price of N2.00 per N1.00 share was approved for the acquisition of the entire 750,000 shares of MOSEL	Cash
9. John Holt Limited (JHL) Public quoted Company	John Holt Investments Limited (JHI) Public quoted Company	1987	A price of N1.70 per 50k share for JHL and N4.00 per 50k share for JHI was approved. The approved prices thus gave an exchange ratio of 235 shares of JHL for 100 shares of JHI	The price of N1.70 per 50k share also applied to the additional issue of 7,178,443 ordinary shares of 50k each to Nigerians in compliance with
10. Standard Breweries Nigeria Ltd. (SBNL)	Private Company United Beverages Limited (UBL) Private	1988	An exchange ratio of 300 shares of (UBL) for 100 ordinary shares of SBNL was approved. Under this arrangement, SBNL was approved. Under this arrangement, SBNL issued 3,333,334 shares of N2.00 each at N3.00 a share in exchange for	Exchange of shares
11. Lever Brothers Nigeria Limited (LBN) Public quoted Company	Cheseborough Products Industries Limited (CPI) Private	1988	An exchange ratio of 83 LBN shares for 100 of CPI was approved. The new shares of LBN consequently issued in exchange was at an approved price of N1.80 per 50k share while a CPI share was at N1.50 per 50k	LBN was to increase its Authorized Capital to enable it issue 7,529,360 shares in exchange for 9,072,000 shares CPI.

Source: Nigerian Securities and Exchange Commission, May, 1989. This table summarizes successful merges in Nigeria from 1982 to 1988. It contains information about the acquiring company, the target company to be acquired, the year of acquisition, the conversion terms and the effects of the merger on the company finance.

Table 2: Successful Mergers in Nigerian Banking Industry in 2006

S/N	Pre Merger/ Consolidation Companies	Post Merger/Consolidation Companies
1	First Bank of Nigeria Plc, MBC International. Bank and FBN (Merchant Bankers)	First Bank of Nigeria Plc.
2	Union Bank Plc., Union Merchant Bank, Broad Bank & Universal Trust Bank	Union Bank of Nigeria Plc
3	United Bank for Africa, Standard Trust Bank & Continental Trust Bank.	UBA Plc.
4**	Zenith Int. Bank Plc	Zenith Int. Bank Plc
5	Intercontinental Bank, Global Bank, Gateway Bank& Equity Bank	Intercontinental Bank Plc.
6**	Guaranty Trust Bank Plc.	Guaranty Trust Bank Plc.
7	Afribank of Nigeria & Afribank Int. Merchant Bank.	Afribank of Nigeria Plc Afribank Nigeria Plc
8	Diamond Bank & Lion Bank	Diamond Bank Plc
9	Oceanic Bank, International & Trust Bank	Oceanic Bank Int. (Nig Plc.)
10	Wema Bank & National Bank	Wema Bank Plc.
11**	Nigeria Int. Bank Ltd	Nigeria Int. Bank Ltd
12	Acee Bank, Marina Int. Bank & Capital Bank Int.	Acess Bank Nigeria Plc.
13	FCMB, Coop. Dev. Bank &Nig-American Bank	First City Monument Bank Plc
14	2nd Round merger with Sterling Bank Plc	Eco bank Nigeria Plc.
15	IBTC& Chartered Bank & Stanbic Bank Nigeria Ltd	Stanbic IBTC Bank Plc.
16	First Atlantic Bank, Inland Bank IMB & NUB	First Inland Bank Plc
17	Prudent Bank, EIB, Bond Bank Reliance Bank & Cooperative Bank	Sky Bank Plc.
18	Magnum Trust Bank, NAL Bank, NBM Bank, Trust Bank & Indo-Nigerian Bank.	Sterling Bank Plc
19	First Interstate Bank, Inter City Bank, Tropical Commercial Bank, Bank of the North, New Africa Bank, Centre Point Bank, Societe Bancaire, Pacific Bank & NNB.	Unity Bank Plc
20	Citizens Int. Bank, ACB Int. Bank, Guiding Express Bank, Omega Bank, Trans. Int. Bank & Fountain Trust Bank	Spring Bank Plc.
21	Equitorial Trust Bank & Devcom Bank.	Equitorial Trust Bank Plc.
	Habib Bank & Platinum Bank	Bank PHB Plc.
22		
23**	Standard Chartered Bank Plc	Standard Chartered Bank Plc
24	Fidelity Bank, FSB Int. Bank & Manny Bank	Fdelity Bank Nig. Plc.
25	Standbic Bank Nig. Ltd.	Standbic Bank Nig. Ltd

*Source: NSE Fact Book (2006): financial Standard Jan.30, 2006 and Nigeria Banking & economy 2008, p. 63. The table shows the successful merger in the Nigerian banking industry in 2006 with the second column showing the pre merger consolidated companies and the third column showing the post merger consolidated banks. ** indicates the five banks that did not merged and stand alone*

The stockholders or owners of both pre-merger companies have a share in the ownership of the merged business and for merger to exist, neither of the participating companies is portrayed as the acquirer or the acquired and both parties participate in establishing the management structure of the combined business. In addition to these features, both companies must be sufficiently similar in size such that one of the participating companies does not dominate the other when combined. According to Weston and Copeland (1989), Merger means any transaction that forms one economic unit from two or more previous ones. It occurs when a corporation and or more incorporated or unincorporated businesses are brought together into one accounting entity. The single entity now carries on the activities of the previously separated independent enterprises. One or more companies may also merge with an existing company or they may merge to form a new company. Merger is also referred to as amalgamation.

A Merger or Amalgamation may be through Absorption or Consolidation. A Merger through Absorption is a Combination of two or more companies into an existing company. Here, the name of one of the companies involved in the merger is retained. A typical example in Nigeria is when United Bank for Africa (UBA) absorbed Standard Trust Bank and retained the name UBA. Acquisition, also referred to as take-over, means the process of combining two or more companies and in which one acquires the assets and liabilities of the other in exchange for cash or shares, goods and or debentures. Section 590 of CAMA, 1990 refers to acquisition as take-over. Accordingly, the CAMA, 1990 defined acquisition as,

"the acquisition by one company of sufficient share in another company to give the acquiring company control over that other company".

Acquisition means all the processes, terms, conditions and fulfillment adopted to purchase a small firm by a big and well established unit. It can also take place through the purchase of stocks and assets of an existing firm. Acquisition can also be seen as all business and arrangements through which the ownership and management of independently operated properties and businesses are under the control of a single management (Ayeni-Agbaje, 2002; Osazee, 2004; Okwuosa, 2005). Acquisitions of companies can be either full or partial. In a full acquisition, the acquirer buys all the stock capital of the purchase company. In partial acquisition, the acquirer obtains a controlling interest, normally above 50% but below 100%. According to Pandey (1997), in acquisition, the target company becomes either a division or a subsidiary of the acquiring company. In the study titled "Effect of Mergers on corporate Performance in India" conducted by Vardhana (2001), compared the pre and post merger operating performance of the corporations involved in merger between 1992 and 1995 to identify their financial characteristics. The findings of the study showed that there was no increase in the post merger profits and that the merging firms were at the lower end in terms of growth, tax and liquidity of the industry. Various studies have shown that most mergers and acquisitions result in failure, yet the concept remains popular, (Virani, 2009). The reasons for the few successes and the many failures remain obscure in the empirical literature. (Stahl, Mendenhall and Weber, 2005).

<u>Review of the Regulatory Framework for Consummation of Mergers and Acquisitions in Nigeria</u>

The statute which provides the legal framework within which mergers and acquisitions can be carried out in Nigeria is the investments and securities Act, 1999. The ISA Act 1999 repealed the provisions of the Securities and Exchange Commission Decree 1988 and also repealed part XVII of the Companies and Allied Matters Act 1990 which contained detailed provisions relating to the public offer and sale of securities, Unit Trusts, Mergers and Takeovers. A much more detailed provisions relating to these and other matters are now in the ISA and the Rules and Regulations issued by the Securities and Exchange Commission (SEC), pursuant to sections 258 and 262 of the ISA (the ISA rules). The major bodies, laws and Acts in Nigeria that regulate the consummation of Mergers and Acquisitions includes, The Investment and Securities Act (ISA) No. 45 of 1999, The Rules and Regulations of SEC (Pursuant to the ISA), The Companies and Allied Matters Act (CAMA) 1990 (as amended), The Banks and other Financial Institutions Act (BOFIA) No. 25 of 1991, The Insurance Act of 2003, Companies Income Tax Act cap. 60 of 1990 (As Amended) and the Rules and Regulations issued by the Securities and Exchange Commission (SEC), pursuant to sections 258 and 262 of the ISA (the ISA rules).

RESEARCH DESIGN AND METHODOLOGY

The research design adopted for this study is the survey method. The choice of survey method is informed by its applicability for collecting standardized data that allows the researcher to create information for precisely answering the how, who, what, where, and when questions concerning the subject matter of the research. Besides, the data structures created, survey methods can increase the researcher's ability to make generalized inferences about the defined target population as a whole. Secondary data were collected from financial statements, reports and Statements of Accounts of ten randomly selected sampled banks. The collected data were analyzed using the Profitability Ratio, Liquidity Ratio and Capital adequacy. In addition to secondary data collected, the researcher conducted personal interviews with a total of twenty (20) banks Chief Executives and Managers of the Sampled Banks.

DATA ANALYSIS AND RESULTS

Impact of Mergers and Acquisitions on Corporate Growth

Mergers and acquisitions stimulated strong growth in the banking sector and the growth indicators in earnings and size of the balance sheet recorded in the first two years of post consolidation are unmatched anytime in the history of Nigerian banking. Triple digit growth in asset size, revenue and profit was recorded in the selected banks. Table 3 shows the number of banks reduced from 89 to 25 while the number of bank branches increased from 3,382 in 2004 to 4,579 in 2007. This implies that consolidation has led to increase in the spread of banks in Nigeria as given by the number of bank branches. The table further shows the total assets base of banks increased from 3,392 billion Naira in 2004 to 10,431 billion Naira in 2007 while total capital reserves reduced from 1,050 billion Naira in 2004 to 957 billion Naira 2006. The liquidity ratio increased from 42% in 2004 to 53% in 2006, with the figures slightly below the 2000 figure of 58%. Finally, the loan-to-deposit ratio shows an increase from 85%, in 2004 to 98% in 2006.

Table 3: Summary of the Impact of Consolidation on Some Bank's Statistics in Nigerian Banking Industry

	Pre –Consolidation Years			**Post Consolidation Years**	
	2000	2002	2004	2006	2007
No. of Banks	89	89	89	25	25
No. of Bank Branches	2306	3132	3386	3468	4579
Total Assets' Base of Banks (N' Billion)	1,707	2,767	3,392	6,738	10,431
Capital and Reserves (N' Billion)	395	822	1,050	957	n/a
Av. Cap. And Reserve per Bank (N' Billion)	443	923	1,180	3,828	n/a
Liquidity Ratio (%)	58	49	42	53	n/a
Loan-to-Deposit Ratio (%)	46	78	85	98	n/a

The table shows total bank performance in Nigeria in the pre-consolidation and post-consolidation years. With the first column showing the performance indicators ranging from the number of banks, the number of bank branches, the total asset base of the banks, the capital and reserve of the bank, the liquidity ratio and the loan-to-deposit ratio. Column two and column three are the pre consolidation years (2000-2004) and the post consolidation years (2006-2007) respectively. Source: Central Bank of Nigeria Annual Report and Statement of Account, 2008.

The operating capacity of each bank was significantly increased through a combination of mergers and acquisitions and new equity capital build up. This increased the revenue and profit capacities of the banks significantly in two years of post-consolidation. Table 4 shows the impact of consolidation in First Bank of Nigeria Nig. Plc. First Bank is one of the largest banks in the country by size of the balance sheet with almost one and half times, (i.e. about 147.8%) from N616,824 million in March 2006 to N1,528,234 million in March 2008. Gross earnings of the bank swelled from N67, 440 million to N155, 725 million during the same period, a leap of 130.9%. The bank's net profit also advanced by 111.0% from N17, 383 million in 2006 to N36, 679 million in March 2008.

Impact of Consolidation on the Sampled Individual Banks

Table 4: First Bank of Nigeria Plc. N' m

Year	Gross Earnings	Net Profit	Total Assets
2004	51,318	11,618	384,211
2005	57,255	13,050	470,839
2006	67,440	17,383	616,824
2007	90,323	18,383	884,804
2008	155,725	36,679	1,528,234

The table shows the impact of consolidation on First bank Plc. Between the post consolidation years of 2004-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. The data was sourced from the first bank's Annual Report Statement Accounts – Various Years

United Bank for Africa is another large bank in the Nigeria banking industry. The banks total assets, as shown in Table 5, which stood at N884,137 million in September 2006 rose significantly by 89.3% to N1, 673,333 million in September 2008, while gross earnings of the bank advanced by 87.4% rising from N90,447 million in 2006 to N169, 506 million in 2008. By the same token, the bank's net profit rose by over 257% from N11, 550 million to N41, 239 million during the same period indicating that UBA's posted a positive post-consolidation performance.

Table 5: United Bank for Africa Plc. N' m

Year	Gross Earnings	Net Profit	Total Assets
2004	24,510	4,525	212,024
2005	26,089	4,921	250,783
2006	90,447	11,550	884,137
2007	109,457	21,540	1,191,063
2008	169,506	41,239	1,673,333

The table shows the impact of consolidation on United Bank for Africa Plc. Between the post consolidation years of 2004-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. The data was sourced from the bank's Annual Report Statement Accounts – Various Years

Table 6 shows the statistics on Intercontinental Bank Nig. Plc. Intercontinental Bank Plc is regarded as one of the largest banks in the post consolidated era. The bank grew its balance sheet size by over 277.1% rising from N369, 232 in February 2006 to N1, 392,210 million in February 2008. Its revenue base was raised from N41, 517 million to N174, 615 million over the same period, an increase of over 320.6% which also reflected in the company's profits as the company's net profit surged upwards from N7, 217 million to N33, 994 million over the same period recording a rise of over 371%.

Table 6: Intercontinental Bank Plc. N' m

Year	Gross Earnings	Net Profit	Total Assets
2003	21,204	3,112	96,858
2005*	32,795	5,703	203,647
2006	41,517	7,217	369,232
2007	87,920	15,121	704,783
2008	174,615	33,994	1,392,210

*The table shows the impact of consolidation on Intercontinental Bank Plc. Within the post consolidation years of 2003-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. The sign * represents the change of accounting year. Source, Intercontinental Bank Annual Report and Statement of Account various years*

Oceanic Bank Plc. also recognized as one of the leading banks in the Nigerian banking industry raised its asset base from N372, 035 million in September 2006 to N1.246, 218 million in September 2008 as shown in Table 7. Gross income rose by 321.2% from N44, 685 million to N188, and 218 million over the same period while net profit grew from N9, 559 million in September 2006 to N17, 532 million in

September 2007 before dropping in 2008, a fall which is largely attributed to the direct impact of the 2007-2008 global financial crisis.

Table 7: Oceanic Bank International [Nig.] Plc. N' m

Year to Sept	Gross Earnings	Net Profit	Total Assets
2004	12,624	3,288	86,884
2005	24,488	5,897	217,803
2006	44,685	9,559	372,035
2007	74,937	17,532	1,038,437
2008	188,218	9,609	1,246,182

The table shows the impact of consolidation on Oceanic Bank International [Nig.] Plc .within the post consolidation years of 2004-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. Source; Oceanic Bank Annual Report and Statement of Account various years

Access Bank is recognized as one of the medium Banks operating in Nigeria as shown in Table 8. The trend from the company's financials shows growth in operating figures was even more spectacular amongst the medium and small banks. Access Bank, for instance, which had a total of N174, 554 million asset bases in March 2006 closed with a balance sheet size of N1, 045,568 million in March 2008. Its revenue base swelled from N13, 359 million to N57, 999 million over the same period. The bank's net profit multiplied from N732 million in 2006 to N15, 881 million in 2008, showing a very strong posting in the post-merger era.

Table 8: Access Bank Nigeria Plc. N' m

Year to March	Gross Earnings	Net Profit	Total Assets
2004	5,515	638	31,342
2005	7,495	502	66,918
2006	13,359	732	174,554
2007	27,881	6,083	328,615
2008	57,999	15,881	1,045,568

The table shows the impact of consolidation on Access Bank Nigeria Plc. covering the post consolidation years of 2004-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. Source; Access Bank Annual Report and Statement of Account various years

Fidelity Bank, which was among the smallest banks in the post consolidation era, registered some of the highest growth indices as shown in Table 9. Its asset base was raised from N121, 089 million in June 2006 to N535, 479 million in June 2008, a growth of over 342.2%. The bank's gross earnings was also raised from N11, 931 million in June 2006 to N42,660 in June 2008, an increase of over 257.6%. By the same token, the net operating profit of the bank was raised from N3, 177 million to N13, 150 million during the same period representing an increase of over 313.9%.

Table 9: Fidelity Bank Plc. N' m

Year to June	Gross Earnings	Net Profit	Total Assets
2004	5,471	914	27,552
2005	6,159	1,237	34,953
2006	11,931	3,177	121,089
2007	24,859	4,437	218,332
2008	42,660	13,150	535,479

The table shows the impact of consolidation on Fidelity Bank Plc. covering the post consolidation years of 2004-2008 with the second, third and fourth columns representing the bank's gross earnings, the net profit and the total assets respectively. Source; Fidelity Bank Annual Report and Statement of Account various years

Impact of Mergers and Acquisitions on Bank Profitability

An assessment of the performance of the sampled banks shows the significant growth in revenue and balance sheet figures was reflected in all the income lines and asset classes of the respective banks. The results are presented in Table 10. High growth in operating figures was industry wide and reflected even in the few banks that did not apply mergers and acquisitions to meet the Central Bank's requirement. The growth drivers in these banks were driven by fresh equity injections. However banks that applied mergers/acquisitions and new equity capital injections generally grew much faster. Therefore, it is safe to infer that there is significant growth in most of the banks after consolidation.

Table 10: Banking Industry Performance Ratios [%]

Indicator	2004	2005	2006	2007	2008
Net Profit Margin	15.0	18.3	20.3	22.4	25.0
Return on Total Assets	2.6	2.2	2.3	3.4	2.5
Return on Equity	20.3	16.4	12.6	15.5	14.9
Net Interest Margin	51.9	59.8	63.5	62.8	65.4
Interest Income/Loans & Advances	24.8	19.0	19.1	15.8	14.5
Interest Cost/Total Deposits	8.1	5.8	4.5	3.8	3.9
Operating Cost Margin	47.7	45.9	47.5	44.3	40.4

The table shows the total banking industry performance indicators in Nigeria over the periods 2004-2008. The major performance indicators reviewed in the first column includes; net profit margin, return on total assets,(ROA), return on equity(ROE), the net interest margin, the ratio of interest income to loans and advances, the ratio of interest cost to total deposits and the operating cost margins of the banks. Source; Source, Nigerian Banking and Economy 2007and 2008

The observed high growth in profit numbers among the post consolidated banks was analyzed further by examining profitability ratios. We found that the banks maintained a trend of improving profitability ratios in the first two years of their consolidation. The ability to convert revenue into profit was consistently improved between 2006 and 2008. Industry average net profit margin improved from 20.3% in 2006 to 25% in 2008. The improvement was traced to the benefits of economic of scale which enabled the banks to streamline costs generally. Rates of return failed to match the high growth in profit as a result of huge equity capital injections in 2005 and 2007. However rates of return were slightly better in 2008 for the industry than recorded in 2006. The ability of banks to improve rates of return even marginally despite huge public offers that extended into a second round was an indication of a slowdown in the overall banking performance in the post consolidation era.

Net interest margin improved among the banks analyzed, indicating a good ability to grow interest income ahead of interest expenses. The consolidation process swept off the marginal banks that used to borrow at penal rates of interest, compelling depositors to accept the low interest structure of the large banks. Also, during the consolidation period, investors withdrew huge funds from the rest of the economy to invest in the banking industry. The injection of huge funds raised the liquidity positions of the banks significantly and led to a reduction interest rates on deposit liabilities. The boom in the economy in the post consolidated environment enabled banks to expand their lending operations rapidly, which saw rapid growth in interest income as well. Excessive liquidity in the hands of banks in the post mergers and acquisition trading made banks compete actively on the asset side of the balance sheet.

This led to rapid expansion of the loan portfolio, which was the main driver of the high growth in the size of the balance sheet. The significantly increased lending capacity of banks and the easier availability of credit even at micro finance level resulted in a general decline in interest income earned from loans and advances. The banking industry average interest income from loans and advances declined in the post merger and acquisition environment from 19.1% in 2006 to 15.8% in 2007 and further down to 14.5% in 2008.The decline in interest income from loans and advances was more than compensated for by the massive increase in the credit portfolio volumes. There was also a corresponding decline in interest expenses due to the high level of liquidity in the system. The average interest rate paid on the naira of deposit liabilities by banks declined from 4.5% in 2006 to 3.8% in 2007 and inched up at 3.9% in 2008. The decline in interest cost was slightly more than the decline in interest income, which resulted in the slight improvement in net interest margin during the period.

Mergers and acquisitions also provided an opportunity for banks to rationalize operating cost by applying the economy of scale benefits. While the operating capacities of the merged banks expanded, the cost of financing the operations grew at a significantly reduced pace. Banks grew revenues faster than costs, which again explains the general improvement in profit margins. Industry average pre-tax profit generated per employee grew significantly from N4.7 million in 2006 to N8.2 million in 2008.

The average operating cost margin for the banking industry declined from 47.5% in 2006 to 44.3% in 2007 and further to 40.4% in 2008, the lowest average industry operating cost margin in many years. This means, banks utilized lower cost to drive bigger operating capacities in the post consolidation era.

Impact of Mergers and Acquisitions on Operating Efficiency

The impact of mergers and acquisitions on the operating efficiency of banks seems to follow a random pattern rather than any identifiable general trend. This outcome seems to reflect the unusual circumstance in which the mergers and acquisition strategy was applied. The policy was applied mainly for regulatory compliance rather than market or business environment driven. There was also an officially dictated time of 18 months within which the merger and acquisition process must be completed.

Meeting regulatory compliance appears to have been a more important consideration in choosing merger partners than improving internal efficiency. Hence banks differed widely in their efforts to integrate the merged entities into the main operating system. It was comparatively much easier for the large banks that acquired smaller banks to achieve operating stability in the post consolidated environment than for the smaller banks that either merged or amalgamated. One or two banks that had similar operating structures before the acquisition found it easier to achieve an integrated operating system than the rest. The worst affected banks could not issue audited financial statements for two to three years after consolidation. These comprise mainly the amalgamated banks that set out to build one bank out of several merger entities with different operating systems and corporate cultural backgrounds.

There were others that were held down by weak partners and therefore could not find their feet long after the conclusion of the merger or acquisition. In the course of the delay in achieving an integrated operating structure, operating efficiency suffered severely. The effort to meet high returns promises made to investors in the process of high equity capital raised in the market did not permit a cautious approach needed to strengthen internal efficiency. Many banks doubled large-sized loan portfolios within one financial year; other assets tripled in some cases and investment assets surged almost without limit. The initial indications were that banks were growing both credit volumes with quality at the same time. The industry average percentage of classified loans declined from 14.8% in 2006 to 11.2% in 2007, dropping to 4.5% in 2008 as shown in Table 11. This outcome contradicted the normal expectation for rapid portfolio expansion to lead to deterioration in credit quality. Apparently, signals of an underlying credit quality problem were ignored until the economy faltered under the global financial crisis.

Table 11: Banking Industry Loan Performance Ratios [%]

Indicator	2004	2005	2006	2007	2008
% of Classified Loans	15.7	12.7	14.8	11.2	4.5
Loan Loss Reserve/Classified Loans	85.3	82.5	82.5	92.8	108.0

The table shows the impact of mergers and acquisition on banks operating efficiency with the major indicators reported in the first column being the percentage of total bank classified loans and the ratio of loan loss reserves to classified loans. Source, Nigerian Banking and Economy 2007and 2008

The improvement in credit quality ratios amid the most aggressive risk portfolio expansion in history is not considered an indication of efficiency in the post merger and acquisition entities. It is seen rather as evidence of reduced efficiency in institutions that began to expand business volume without first achieving operating stability. Banks competed to grow their loan portfolios aggressively without having in place effective machinery for recovery of bad assets an indication that mergers and acquisition did not result in the creation of effective risk management model in banks.

During the financial crisis that followed it was observed that only two banks that applied caution in growing business volume were least affected by the problem of huge credit losses that hit the banking industry adversely. The poor risk management quality is traceable to regulatory disposition that governed the consolidation process. The main objective of the regulatory authorities is to build large banking institutions that would become visible in the global market place. The Central Bank created some incentives such as external reserve management opportunities for banks to build the size of their balance sheets. Consequently, a number of banks did first and second round large equity offerings in the capital market after concluding mergers and acquisitions. It is apparent that in a bid to drive competitive size building capacities in the banking sector, operating efficiency suffered greatly. This position is further corroborated by the finding of Nigeria Banking & Economy 2009 – a banking industry report that the observed improvement in credit quality of the banking industry was not a reflection of progress in recovering bad assets. It showed that the improvement is an outcome of a more rapid growth of the gross loan portfolio than non-performing loans. That situation placed many banks in precarious positions when a large proportion of hitherto good accounts were swept into the bad debts portfolios in 2009.

A number of banks faced challenges of becoming big almost over night. They faced the hurdle of how to manage size and defend quality at the same time. Nigeria Banking & Economy had in 2006 noted that being big and efficient are not known to go together and saw the need for banks to develop firm strategies to deal with the challenges of becoming large institutions.

<u>Post Consolidation Crisis in the Banking Sector in Nigeria</u>

Following the global financial crisis of 2007-2008 which had its root in the mortgage crisis in the US, the banking industry in Nigeria was faced with significant pressures which led to financial crisis and bank distress. A risk management audit conducted by the Central Bank in 2009 revealed serious health problems in many banks, which necessitated a ₦620 billion bail-outs of the worst affected banks in September 2009. Massive credit losses were recorded by all the banks in operation, which wiped out reserves and sank equity capital of a number of banks into negative, as shown in the table 12 below.

Table 12 shows the extent of loss of individual banks in terms of negative equity capital recorded by the banks in the wake of the global financial crisis. As at end December 2009, all banks with the exception of Unity bank Plc. recorded a negative equity capital. The importance is that financial distress, which the regulators sought to cure through mergers and acquisitions, has returned into the banking system at a bigger dimension. In the present dispensation, the big banks suffered more in terms of distress than the small, marginal banks that either merged or closed. The analysis also revealed the serious health problems of banks have also been traced to the existence of a high level of indiscipline and fraudulent activities on the part of top level management of banks.

A number of former management executives of banks were deposed by the Central Bank and are presently facing trial for massive fraudulent deals. The amounts involved are several multiples of the figures for which any previous bank official has ever been charged. The expectation of the Central Bank was that big banks will be less inclined to indulge in sharp practices, unethical conduct, fraud or flouting of regulatory rules. The actual position as revealed by this paper is that the bigger the bank, the bigger is the size of fraudulent deals, the level of financial recklessness and capacity to play contrary to the rules of the game.

Table 12: Capital Deficiencies in Rescued/Weak Banks – December 2009

Bank	Equity Capital (N, Billion)
Intercontinental Bank	- 380.0
Afribank	-258.1
Union Bank	-238.3
Bank PHB	-194.6
FinBank	-125.9
Oceanic	-115.9
Wema Bank	-45
Unity Bank	0.7

The table shows the extent of capital deficiencies of the merged banks in 2009, with only one bank, Unity Bank recording a positive equity capital of N.7 billion. Source; Data trust

CONCLUDING COMMENTS

This paper examined the effects of mergers and acquisition on corporate growth and profitability. In particular, it set out to answer the research question of whether merger and acquisition is the best solution to bail out organization in financial crisis using Nigeria as a case study by simply analyzing the pre-banking sector consolidation era and the post-banking sector consolidation era in Nigeria. The paper tested propositions raised in the introductory section by using a simple survey method and drawing from secondary data collected from the financial statements, reports and Accounts of ten (10) sampled banks selected randomly out of the existing twenty five (25) recapitalized banks over the periods 2004-2008, with data collected covering the pre-merger and acquisition ear and the post-merger and acquisition era in the Nigerian banking industry. In carrying out the test, we analyzed the impact of bank consolidation on each of ten sampled banks, the entire banking industry performance ratios over the sample periods and the capital deficiencies in the recapitalized banks in the post consolidation era.

The paper concluded that, mergers and acquisitions served the objective of regulators to cure the banking system of financial distress only on a temporary basis. The analysis found that the expectation that building large banks through mergers and acquisition would provide a permanent solution to financial crises in the banking industry has not been realized. Given that, two years after the conclusion of mergers and acquisitions exercise in Nigeria, financial distress returned with an alarming proportion to the banking sector. In the immediate post merger environment, four of the banks could not find their feet and remained virtually distressed, warranting regulatory intervention in their operations.

The paper revealed the Central Bank's policy of consolidation under which mergers and acquisitions were applied has some fallout that made the industry vulnerable which includes amongst other things; the straight jacket policy of banking consolidation that prevented banks from specializing in various aspects of the financial services market, the seemingly over concentration and homogeneity of the products offered by all the banks in the industry and the lack of linkage between the banking sector and the real economy. About 70% of the executives interviewed agreed that the effect of merger and acquisition on shareholders is that the shareholdings will be diluted and dividend ratios will also be affected.

Also management style and structure will also change. From the overall analysis, it is found that merger and acquisition, if well consummated will increase banking sector profitability and enhance corporate efficiency but it is certainly not the best solution to bail-out corporate organization that have fallen deep into financial crises in a developing country where the financial sector has not attained an advanced and sophisticated stateOne of the limitations of this study is the use of banking sector performance indicators to analyze the effects of merger and acquisition on profitability and banking sector efficiency rather than us use testable time series data that would have allowed us develop a testable model. In addition to this limitation is the lack of linkage between the capital market and the collapse of the banking sector in the post consolidation years. Future research will seek to address these short comings by attempting to build an appropriate model to ascertain if the capital market collapse was actually responsible for the banking sector crisis that necessitated a bail-out fund of N620 billion and not the merger and acquisition as claimed by this paper.

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