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Full Length Research Paper

The Impact of Consolidation on the Performance of Banks in Nigeria

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This study evaluates the impact of consolidation on the performance of banks in Nigeria. The study used a period of 12 years from 2000 to 2011 comprising six years pre and post consolidation era. The population of the study is (22) banks in which four (4) banks are drawn using stratified sampling technique. The study utilizes secondary data obtained through annual reports and CBN banking supervision. T-test was employed to test the hypothesis formulated. The findings of the study show that consolidation has significant positive impact on the performance of banks in Nigeria. The study therefore recommends that the management of banks should work hard to ensure that adequate measure is being put in place to determine increasing rate of return on asset, return on equity and net profit margin of their banks reform of this nature such as consolidation of banks is one of the ways to improve the banking sector financial stability.

Keywords: Consolidation, Banks, Performance

INTRODUCTION

Consolidation in the banking system is a global phenomenon, which is said to have started in advanced Economies. Notable examples of countries experiencing a wave of mergers and consolidations in the banking industry in recent times are the United States of America (USA) and Japan (Hall, 1999). According to Kwan (2004), since the enactment of the Riegle-Neal Act, which allows interstate branch banking beginning from 1997, the Number of large bank mergers in the USA has increased significantly. Today, the U.S.banking sector is reported to be in good shape, with record profits and relatively low Volumes of problem loans. Further research on mega mergers in the USA suggests that Merged banks experienced higher profit efficiency from increased revenues than individual banks, due to the fact that they provide customers with high value added Products and services (Akhavin, Allen,Berger, David and Humphrey 1997).

The need for a strong, reliable and viable banking system in Nigeria is under scored by the fact that the industry is one of the few sectors in which the shareholders' Fund is only a small proportion of the liabilities of the enterprise. It is, therefore, not surprising that the banking industry is one of the most regulated sectors in any economy. It is against this background that the Central Bank of Nigeria, in the maiden address of its past Governor, Prof. Charles Soludo, outlined the first phase of its banking sector reforms designed to ensure a diversified, strong and reliable banking industry. The major objective of the reforms is to ensure and guarantee an efficient and sound financial system. Thus, the reforms were designed to enable the banking system develop the required resilience to support the economic development of the nation by efficiently performing its functions as the medium of financial intermediation (Lemo, 2005). Also, these reforms were to ensure the safety of depositors' money, position banks to play active developmental roles in the Nigerian economy, and become major players in the sub-regional, regional and global financial markets.

Historically, the Nigeria banking industry has undergone four stages of development phases. The first stage could be described as the unguided liaises fair phase 1930 to 1958, during which several poorly capitalized and unsupervised indigenous bank failed before their tenth anniversary. The second stage was the control regime 1960 to 1985, during which the central bank of Nigeria ensured that only fit and proper banks were granted a license. The year 1986 witnessed tremendous change in the nation's financial landscape. This was as a result of the economic reforms embodied in the structural adjustment programmed (SAP) that marked the introduction and commencement of neo-liberal philosophy of free entry from being in operation which was over stretched and banking license were dispense by the political authorities on the basis of patronage . This reform however, led to the growth in terms of number of banks, branches, product creativity and the level of operation of Nigerian banks. This was the third phase which was referred to as the post-SAP, the control regime 1986 to 2004 (Ekezie, 1997).

However, from 1987 to 1989, there were series of fluctuations experienced in the foreign exchange market and insider abuses in the Nigerian banking industry. The end result was the massive close down of banks that began to set in mainly due to poor corporate governance non- compliance with regulations, weak management and declining profits, capital efficiency, insolvency, high incidence of nonperforming loans/poor asset quality , and over reliance on foreign exchange market for income through round tripping of officially sourced foreign exchange (Yakubu, 2008).hence the need for a reform in the banking system.

Mergers and Acquisition which are divisions of consolidation are commonplace in developed countries of the world but are just becoming prominent in Nigeria especially in the banking industry. Before the recent consolidation, the Nigerian banks had not fully embraced mergers and acquisitions as expected because of their cultural background in terms of asset ownership, greediness, shame, fear of what people will say and lack of proficiency required for mergers and acquisitions, among other reasons. The issue of mergers and acquisitions in banking industry started in October, 2003 under the past president of CBN (Charles Soludo). The CBN rolled out incentives to encourage weaker banks adopt mergers and acquisitions. The incentives included concessionary cash reserve ratio for a period of two years to the newly restructured banks, conversion of overdrawn positions of weak banks to long-term loans with concessionary interest and the acquired banks could be given up to 24 months grace period for complying with the minimum liquidity ratio requirement to enable it settle down as a newly recapitalized/restructured bank. Though, most of the feeble banks were unwilling to comply until the new order on July 6, 2004 (Famakinwa et al, 2004). The situation changed from July 6, 2004 as many banks had either merged with or acquired other banks.

The increase in awareness and scheme is due to a number of reasons such as threat of distress, regulatory driven environment, foreign inducement, persuasion from regulatory bodies and economic benefits of mergers and acquisitions. The most common of these factors that is responsible for the growth of mergers and acquisition in Nigerian Banks is regulatory factor. Thus, mergers and acquisitions as consolidation tools have become a near permanent feature of our financial system after July 6, 2004 (Ewubare, 2004). The policy of 25 billion naira minimum capital base forced banks to go into merger and or acquire one another as a strategy to meet the requirement. Part of the broad objectives of consolidation expected include improvement of profitability and efficiency of the banks in terms of operations and finance.

The objective of this paper is to assess the impact of consolidation on the performance of listed deposit money banks in Nigeria. The study also seeks to examines the impact of consolidation on Return on Asset, Return on Equity and the contribution of consolidation on Net profit margin of listed deposits money banks in Nigeria.

While it seeks to address the following question which emanates from the objective: what is the impact of consolidation on the performance of banks in the Nigeria?

The paper has the following hypothesis:

Ho_1: Consolidation has no significant impact on Return on Asset of listed deposit money banks in Nigeria

$Ho_{2:}$ Consolidation has no significant impact on Return on Equity of listed deposit money banks in Nigeria

Ho_3: Consolidation has no significant impact on Net profit Margin of listed deposit money banks in Nigeria

The scope of the study is restricted to assessing the impact of consolidation on the performance of listed deposit money banks in Nigeria. The time frame of the study is 2000 to 2011 (six years pre- consolidation period and six years post consolidation period).The data on Return on Asset (ROA), Return on Equity (ROE) and Net Profit Margin (NPM) are collected in order to examine the impact of consolidation on the performance on listed DMBN.

Review of Related Studies and Theoritical Framework

Several literatures were reviewed to find the empirical positions arrived at by the researchers. Usman (2008) studied the impact of consolidation on performance, proxies performance as efficiency and profitability between the period 2003 to 2008.The finding show that consolidation has impacted on both profitability and efficiency but not significant. Sanni, Ebo and Adereti (2012), reported a positive significant difference between earnings per share of nine banks, following their study of post consolidation on profitability in Nigeria, using a time frame of 2006 to 2010, also employing cumulative earning per share as the profitability (performance) measure. Similarly, Adegbaju and Olokoyo (2008), considered recapitalization and bank performance, using yield on earnings asset, return on asset and return on equity as performance proxy. The study found a positive significant relationship between recapitalization and profitability (ROA and ROE) and a negative significant relationship with yield on earning asset (YEA).

Furthermore, the study by Ritu, Pablo, David and Raul (2004) reported a strong positive significant effect of bank consolidation on bank performance, which implies that bank return increases with consolidation. However, the reverse is the case with insolvency risk which is reduced. The study was conducted in Argentina, within the period 1995 to 2000 also taking return on asset and return on equity as the proxy for performance. The results also suggest that there are other factors; both macro and bank specific that affect bank performance. Umoren and Olokoyo (2007) also found return on equity to be positively and negatively significant to asset profile and capital structure of a bank which were used as proxy for consolidation in their study of merger and acquisition in Nigeria, analysis of pre and post consolidation between 2006 to 2008. In addition, Onikoyi (2012), study merger and acquisition on bank performance in Nigeria (UBA and SKYE banks) and reported a strong positive relationship between consolidation (shareholders' fund) and performance (total assets).

Brown and Modiff (1988), Lichtbery and Siegel (1990) report negative effects of the merger and acquisitions on employment in the USA. It is important to note that part of the evidence is based on the very restricted samples of the companies covering narrow segments of the US economy, for instance, Brown and Modiff (1988) obtain their estimates on the effectof merger and acquisitions on employment from a sample of companies located in the state of Michigan's for the period 1978-1984. This may be thereasons for somewhat mixed results on the employment effects of mergerand acquisition that have emerged from the USA.

According to Conyonget al., (2000a, 2000b, 2000c), reports a negativeeffects of the mergers on the employment in the UK. By using data on the277 listed companies over the period 1967-1996. Interestingly, the negative effects on the employment are particularly pronounced for related and hostile transactions. Girma and Gorg (2004), discover by using data from the

The UK electronics industry for the period 1980-1993 reports that the incidence of foreign takeover reduces the employment growth of a domesticestablishment, in particular for unskilled labor. Hence, cross-border merger and acquisition have some effects on the determination of skill-mix incompanies. Merger and acquisition decrease the number of independent players which concentrate the markets. Salant et al (1983) and Perry and Parter (1985) have shown that it does not pay to purchase another firm in order to decrease competition and or gain pricing power in the standard competition. However deviating from the framework, the positive effect of decreasing the number of players on profit is, in any case, present in horizontal merger andacquisitions. Therefore, the tendency to internalize the strengthened market power by higher prices will be part of the horizontal merger and acquisition and one can expect that, for this part, merger and acquisition will reduce thescale of the production and labor impact too.

Amel et al (2003) viewed that consolidation may enhance revenues although results vary with countries and deals analyzed; moreover, the gains appear limited in magnitude. The evidence for Europe suggests that the more efficient banks tend to acquire institutions in worst shape that is why they will not get as much as possible gains.Vender vanet (1996) finds that domestic mergers of equals in EC countries have a positive impact on profitability, mainly driven by improvements in operational efficiency. Akhaent et al (1997) find little change in cost efficiency but an improvement in profit efficiency of large US banks after merger and acquisition, especially if the merger participants were relatively inefficient prior to the merger. Usually Profit cannot be improved until efficiency is improved, but this study finds that only profit improves.

Berger (1998) finds similar results in a study that includes all US banks mergers, both large and small, from 1990 and 1995. Haun (1996) assesses the success of mergers along five characteristics, namely, size, operational results, services, liquidity and profitability. He reported that the operating profitability decreases after the merger due to increased personnel costs. In addition, the assets growth as well as the amounts of total revenues worsens in the year after the merger, the results of regression analyses provide evidence that mergers had a positive effect for those of the involved banks with worse performance before the merger. But as usual, a year after merger banks are not making profit, but subsequent years will be profitable.

Williamson (1970) argues that companies like the Multi-Bank Holding Companies usually outperform differently structured competitors. The researcher particularly emphasizes the role of the decision power allocation between the center and the subordinate levels. Cost savings and x-efficiency gains could vary depending on which functions and decisions are decentralized and which remain at the center. Newman and shrives (1993) test Williamson's hypotheses by analyzing the performance of over 1700 banks of different organizational forms. They divide the banks into four revenue groups, and estimate efficiency measures for each bank in the groups. The author finds that the multi-bank holding subsidiaries are more efficient than one-bank holding structures in the middle of two revenue groups. Banks, in the largest revenue group, are not found to differ substantially in efficiency

There are a few studies on the effects of inter-company bank mergers.Linder and Crane (1993) find out that in more than three-quarter of the 25inter-company bank mergers they studied the returns on assets increases inthe year following the merger and this improvement is sustained in thesecond year as well. Non –interest costs to assets, however, also increaseafter the merger compared to non-mergers pears. Thus, this study fails toprovide simultaneous evidence on the both profitability and cost efficiencygains of inter-company mergers. But in respect of Nigeria, let us test thisHypothesis that, Ho there no significant impact of bank consolidation on theprofitability of Nigerian banks.

De yong (1993) studied 348 banks mergers of which 43 percent were inter-companyones. The author estimates pre- and post-merger cost efficiency byapplying a thick frontier approach. Prior to merger, the acquiring bank wasmore cost efficient than the target in only 42 percent of the intra-companymergers. However, in the three years period after the merger, cots efficiencyimproved in about 64 percent of the cases. Elsas (2004) finds out a strongrelationship between the financial performance of target banks and mergerdecisions among 3600 German savings and cooperative banks. Most of thetarget banks were in financial distress with large amounts of non-performingloans. The distress mergers in these cases usually resulted in portfolioimprovements and a reduction of a bad loan provisions. In the medium term,however, a decrease in profitability was also registered. The overall post merger efficiency effects are considered satisfactory, having in mind theincentives behind most of the studied mergers.

Evanoff and Ors (2009) also evaluate profit efficiency changes in themarkets following merger activity. The researcher again uses efficiencyrankings to evaluate changes in the relative position of banks. Results for thefull sample and alternative sub samples are presented. Profit efficiency waseither deteriorating or remaining relatively unchanged following marketmerger activity. This could result from an increase in price, competitionhaving significant effects on revenue, efficiency as banks may suddenly berequired to charge more competitive loans rates or transaction fees than werepreviously charged. Combined with the cost efficiency finding, these suggestthat the adverse revenue effects were quite significant.

Park and Pennacchi (2007) find out consolidation result to large multi banksimpact on small banks profits are case specific. It is unsurprising thatempirical research on this issue is mixed. Whalen (2001) finds shares of their msa's between 1995 and 1996. Pill off (1999breports that small banks profits in non-mesa's rural countries increased with the presenceof large multi banks. Using 1985 data for msa's and rural countries of eight unit banking states wolken and Rose (1991) find that small bank profitsdeclared with large multi banks market share.

Berger et al (2007) show that a greater large multi banks market shareincreases, but small bank profitability during 1980s decreased it during1990s. The surmise that technological progress in lending allowed largemulti banks to more efficiently compete with small banks in recent years.

Hannan and Prager (2006b) reported that during 1996-2003 an increasedpresence of large multi banks reduced small bank profits in non-msacountries but not in the less concentratedmsa's. Consistent with our model, they find that impact of large multi banks in reducing small banks profit isthe greatest in the most concentrated non MSA countries. The theory of proportionate effect, Agency theory and marginal proportionate effect theories were all utilized in the context of this study. We have thus found some level of conformity with many of those theories with also, some contradictions.

METHODOLOGY

The research methods adopted for this study is the descriptive method. The population of this study is made up of the twenty - four (24) deposit money banks in Nigeria available as at December, 2011. While the sample size is four (4).The number was reached through the use of filters which are; banks that have actually experienced either merger or acquisition and with strong capital base.Thus, they are arrived at by taking the three banks with capital base of over 200billion which are first bank of NigPlc, Union Bank of Nig. Plc and Zenith Bank plc. And the one bank from the group of banks that have capital base of more than 100billion but less than 200billion which is Guaranty Trust Bank plc (Banking supervision Annual Report, 2005). The data collected and utilized by the study are secondary data extracted from the annual reports and stock exchange fact book. The data are analyzed using T- Test for independent samples. Percentage change of returns on asset, return on equity and net profit margin were used to represent

Table 1.1. Consolidation and Performance of Deposit Money Banks in Nigeria

CON		N	Mean	Std.Deviation	Std.Error Mean
ROA	1.00	28	3.0232	8.62294	1.62958
	2.00	28	3.4300	16.02417	3.02828
ROE	1.00	28	8.65160	8.65160	1.63500
	2.00	28	8.2991	8.29991	1.568454
NPM	1.00	28	.2132	.10011	.01892
	2.00	28	.9168	3.80994	.72001

Source: Result of the SPSS output.

performance. While consolidation is consider from the angle of shareholders' fund and debt (total capital). The justification for the use of this tool of analysis is help us compare the pre and post consolidation means to allow us draw a conclusion on the impact of consolidation.

RESULTS AND DISCUSSION

The hypothesis deals with whether consolidation reform has significant impact on the performance of Nigerian banks or not. The hypothesis was tested using T-test.

Data Analysis

Table 1.1 clearly shows that the mean value for Return on Asset before the introduction of consolidation is 3.0232, while, the mean value after the introduction of the policy (consolidation) is 3.4300. This shows that consolidation as a policy introduced by the central Bank of Nigeria in the year 2005 has positively and significantly impacted on the Return on Asset. This implies that the introduction of consolidation which led to concentration in the banking sector by limiting the number of banks listed in Nigeria stock exchange has brought about an increase in the Return on Asset of listed Deposit money Banks by about 0.41. This may be as a result of the merger and acquisition that take place within this period of the introduction of the consolidation policy which led to the increase in the asset size of the merging or acquiring banks which is also expected to be translated in their return on the usage of such assets of merged banks or acquiring banks.

The result therefore provides an evidence of rejecting the null hypothesis one, of the study which states that consolidation has no significant impact on the Return on Asset of listed Deposit Money Banks in Nigeria. The finding is therefore in line with those of Hughes, Lang, Mester and Moon (1999) while the findings are contrary to that of Akhavein, Berger and Humphrey (1997).

The mean value for Return on Equity before the introduction of consolidation is 8.65160, while the mean value after the introduction of the policy (consolidation) is 8.2991. This shows that consolidation as a policy introduced by the Central Bank of Nigeria in the year 2005 has positively and significantly impacted on the Return on Equity of listed deposit money banks in Nigeria. This implies that the introduction of consolidation which led to concentration in the banking sector by limiting the number of banks listed in Nigeria Stock Exchange has brought about a decrease on the Return on Equity of listed Deposit Money Banks by about -0.352. This may be as a result of the merger and acquisition that take place within this period of the introduction of the consolidation policy which led to increase in Equity of the merging or acquiring banks which the effect is expected to be seen in their return in usage of the equity of merged banks or acquiring banks.

The result therefore provides an evidence of rejecting null hypothesis two, of the study which states that consolidation has no significant impact on the Return on Equity of listed Deposit Money Banks in Nigeria. The finding is therefore in line with those of Spindt and Tarhan (1993) while the finding is contrary to those of Sawada and Okazaki (2003).

Table 1.1 above shows that consolidation impacted on the Profitability of Nigeria Deposit Money Banks, because the mean value of Pre- consolidation period is 0.2132 which is less than that of post consolidation 0.9168. It reveals that banks made more profit after consolidation. The implication is that consolidation had positive impact on the profitability of listed Deposit Money Banks in Nigeria. This also implies that the introduction of consolidation which led to concentration in the banking sector by limiting the number of banks listed in Nigeria Stock Exchange has brought about increase in the Net Profit Margin by about 0.70.

The result therefore provides an evidence of rejecting null hypothesis of the study which states that consolidation has no significant impact on the Net Profit Margin of listed Deposit Money Banks in Nigeria. The findings is therefore in line with those of Vender and Amel (2003) while the findings is contrary to that of Evan off and Ors (2002)

CONCLUSIONS AND RECOMMENDATIONS

The study concludes that consolidation reform in the Nigeria banking sector has impacted positively on Return on Asset and Net Profit Margin, but does not impact positively on Banks Return on Equity. Therefore, consolidation in the banking sector has impacted positively on their performance. It is however, recommended that such initiative should be highly appreciated by banks and the apex banks should force banks to recapitalize once in a while.

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