



Research Article

Impact of Mergers and Acquisition (MA) on performance of Ghana's banking industry

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Abstract

Mergers and Acquisitions (MA) have been of serious concern in financial markets all over the world. The topic is about the desire of firms to acquire others, or join forces together. Some of these transactions have been successful; others unfortunately less so. The rationale for the current study is to investigate the impact of MA on performance of Ghana's banking industry, with emphasis on Societe Generale Bank Ltd. The main data for our study consist of official documents of the bank and the Bank of Ghana like their annual reports and other financial information of several years. These are supplemented by discussions with selected senior officials of the bank. Adopting the Financial Performance (FP) Approach, analysis of data using Microsoft excel package was done. Important findings include: Societe Generale appears to have chalked some modest positive financial performance. Secondly, the results appear to suggest lack of any evidence of costs reduction and operational efficiency. But the study notes that success of the merged company depends on probability of occurrence of staff hostility; insufficient preparation for the evolution; inability to integrate personnel and systems; and irreconcilable differences in corporate cultures and management, all of which must be effectively handled to maximize success of MA activities in the banking industry.

Keywords: mergers and acquisitions, costs reduction, operational efficiency, financial performance, structure- conduct-performance (SCP) paradigm, efficiency hypothesis

INTRODUCTION

Background to the study

Financial markets have been witnesses to many MA over the years. Such MA transactions are almost of daily occurrences all over the world. The advanced countries of the USA and Europe have witnessed periods of high merger activity known as merger waves in the periods: 1897-1904; 1916-29; 1965-69; and 1984-89; with the most current one beginning in the early 1990s. In the United States, MA have been instrumental in the decline in the number of banking institutions: between 1980 and 1997; decreasing from 12,333 in 1980 to 7,122 in 1997. Similar trends have been experienced in Europe.

Some transactions of MA have also taken place in Ghana, the first of which is Societe Generale, our choice of study. Societe Generale resulted from a horizontal merger between Social Security Bank (SSB) and National Savings and Credit Bank (NSCB) in May, 1994. Other MA transactions have been experienced in Ghana, namely, Eco Bank in 2000, Access Bank in 2011, and United Bank of Africa in 2012.

Benchmark analyses based on comparative share performance one year after deal completion found that only 17 percent of deals had actually added value to the combined company, 30 percent had produced no discernible difference, and 53 percent had actually destroyed shareholder value. Companies focusing attention on finance or legal

issues (to the detriment of other areas) were found 15 percent less likely than average to have a successful deal. This brings us to a consideration of:

Statement of the Problem

The question then is whether or not Societe Generale in Ghana has fared much better after having gone through such an MA experience in the light of difficult performances by some institutions across the world. The results of the study could provide a useful pointer and guide to similar banking institutions intending to go through such related transformation.

Objectives of the Study

The specific objectives of the study are to:

- Examine the synergies for such horizontal integration transactions in the financial sector, especially, MA transactions among financial institutions; and
- Analyse whether Societe Generale has been better off with regards to financial performance and cost efficiency.

Significance of the Study

The study will offer an insight into the reasons for the recent growth in MA activities especially among banking institutions. It should also contribute to the existing body of knowledge on MA, and provide relevant material to academia for future research on related matters. Lastly, the results of the study will be significant to the government with respect to policy making as well as the financial markets players, both locally and abroad, who may like to consult the study as reference material.

Scope and limitations of the study

Societe Generale has been chosen for the study due to, firstly, the relatively much easier availability of relevant data for the study as well as the willingness of the institution to cooperate with researchers. The location of our study is Accra, the head office where most of the requisite data will be obtained. This could provide some advantage of time saving with respect to questionnaire administration and collection of relevant data for the study. The study appears specific to Societe Generale, but other institutions must exercise great caution when considering the feasibility of adopting the results of the study.

Organization of the Study

We consider the study under five sections. Section one, the current section is the introductory section; section two provides a review of relevant literature; the third section looks at the organization of data, and details of the research design; section four deals with the analysis and discussion of the results of the research; the last section five examines the major findings of the study, draws up conclusions, and makes relevant recommendations.

LITERATURE REVIEW

Most of the literature on the impact of bank mergers and acquisitions has concentrated on testing the validity of two reciprocal hypotheses. The "efficiency hypothesis" states that the merged bank might reach economies of scale and other efficiency gains and transfer these to the customers in the form of more competitive prices, (Moore and Frederick, 1959). The other, "structure-conduct-performance (SCP) hypothesis", states that a merged firm may exploit its increased market power and impose higher prices, (Mason, 1939; Bain, 1951; 1954)

A paper by Berger and Hannan (1989) presents a first step in testing these hypotheses. In a static study of the relationship between local banking market concentration and deposit rates, Berger and Hannan found out that more concentrated deposit markets are characterised by lower deposit rates. This result supports the SCP hypothesis that ultimately leads to increase in market power.

This position was challenged by Focarelli and Panetta (2003) and Rhoades (1998) on grounds that previous studies only examined a very short period after the merger, and that efficiency gains need more time to realize results. Their conclusion was that efficiency gains could result in the transition period, say up to three years. But in the long-run deposit rates of merged banks could rise and even above those of rival banks, and that the rivals do not change their deposit rates.

Proponents of financial sector consolidation argue that institutions need big size to spread growing information technology and processing costs over larger revenue bases and greater market capitalisation. Consolidation was also being championed by smaller countries to counter growing competition from larger institutions in neighbouring countries. Supporters of MA allege that they facilitate synergies between merged organisations, generate efficiency improvements, increase competitiveness, and enable financial operators to provide services at lower prices. Contending that MA improved efficiency is thus central to making the case for the consumer benefits of mergers and in assessing their potential impact on consumers.

Researchers have identified some factors that drive MA transactions as value-maximization, managerial ego, the need to reduce uncertainty and defensive considerations (acquire to avoid being acquired; ensure that growth keeps up with those of competitors, among others). High levels of corporate reserves and share valuations are among the motives behind consolidation in financial services. The contention is that mergers, by increasing economies of scale and spreading costs over a larger customer base, enable financial operators to provide services at lower price. A case is made for the consumer benefits of mergers by assessing their potential impact on consumers through efficiency improvement. If MA improve efficiency, then larger, combined firms may be expected to pass some savings on to consumers through lower prices or improved services.

But a contrary view contends strongly that their consumer gains only result in employment losses and diminishing access to services. Employment generation of small businesses as benefit from mergers has met with strong opposition. Studies have indeed revealed that larger financial institutions tend to charge more and higher fees than their smaller counterparts and denote an inverse relationship between the sizes of financial institutions and their loan portfolios to small businesses. Alleged benefits like size generating economies of scale able to compete in global markets have also been argued against as they contend that size is irrelevant to international competitiveness and cross-border mergers. There are those who believe that efficiency-based arguments in support of MA confuse size, cost-cutting and efficiency. Rhoades (1987), explains the distinction between efficiency improvements and cost-cutting as: "reductions in operating expenses may result from cutting employees, closing branches, consolidating headquarters offices, closing computer and back office operations and so forth. Such reductions in expenses, however, do not automatically translate into improvements in efficiency as measured by an expense ratio, such as expenses to assets or revenues. Reductions in expenses may be accompanied by corresponding reductions in assets and revenues, which simply represent shrinkage of the firm rather than efficiency improvements". He maintains that the failure to distinguish between cost-cutting and efficiency gains may partly explain the continuing disagreement between bankers "who emphasize the cost reductions to be achieved through mergers" and researchers "who generally study the efficiency effects of mergers".

Two distinct approaches have been identified in the area of value creation by Rhoades (1994), Focarelli and Paretta (2003), Yeveer et al. (2001), Saibu (2012), and Caruso and Palmucci (2008).

The first is based on financial performances of firms using accounting information (data) referred to as Financial performance approach (FP); the second applies to the event-study methodology. While the first approach investigates the ex-post changes in indicators of profitability such as Return on Equity (RoE), or cost ratios, (Cost/Income), the event studies rather analyze the target firms' stock returns in the period when it is supposed the information reach the market.

The FP method adopted in most MA transactions in recent times appears to identify shareholder maximization as the main objective. Researchers like Boot (2003), Amel et al. (2004), Cavallo and Rossa (2001), and Campa and Hernando (2006), have all written on the topic and yielded varied results.

Studies tracking shareholder returns for every large, publicly traded North American acquirer in the 1990s showed that only 44 percent of deals initiated by these companies yielded superior investor returns. On average, acquirers underperformed their respective industries by 3 percent.

For example, shareholder value was an important element in the failed merger attempt between Germany's Deutsche Bank and Dresdner Bank in 2000. Early adopters of shareholder-value goals include Lloyds-TSB and banks in Scandinavia, Spain and the Benelux countries. In 1999, ABN-AMRO of the Netherlands announced a policy shift to shareholder value, requiring greater focus on the expansion of highly profitable activities like asset management; private banking and corporate finance, all of which require only relatively limited capital.

A number of obstacles have been identified as limitations to the progress of MA in the banking industry. A 1993 ILO study on banking noted that efficiency improvements through mergers were frequently overestimated. Contemporary research appears to confirm this observation. Worldwide, two-thirds of mergers end in failure – some because of staff hostility and others because of insufficient preparation and inability to integrate personnel and systems. Even more failures are due to irreconcilable differences in corporate cultures and management. Among some of these obstacles to MA are bank regulation, competition policy, trade union organization, internet banking, and inadequate assessment of cultural aspects of MA: each poses a limitation on effective growth of MA in banking. For example, bank regulation places a limitation on MA to ensure that a merged institution does not exceed the legal size to assume the position of a relatively giant monopoly, as stipulated by law. Also, a 1999 KPMG study noted that MA deals were 26 percent more likely than average to be successful if they paid satisfactory attention to cultural issues, and that a company increases its

chances of success if it uses reward systems to stimulate cultural integration or cooperation. Cultural aspects therefore constitute a significant obstacle to cross-border combinations even though the differences continue to ease with time, education and training. Any merger or acquisition is a complex process taking up more time than usually expected: it requires integrating very different organizations, blending often very diverse cultures and dealing with complex questions of dissimilar work organization. This requires high levels of managerial capacity in change management, the constitution of effective teams and network integration – all demands for which many managers are ill-equipped but which can lead to an accumulation of critical errors, misunderstandings and ruin that might look like a highly promising deal on paper!

Developed countries are the most important sellers and buyers in MA, accounting for about 90 per cent of sales/purchases in 1998-99. Of about 10 per cent of sales/purchases involving developing countries, the bulk (70 per cent) originates in Latin America and the Caribbean. The value of mergers and acquisitions' sales by developing countries increased from \$12 billion in 1991-95 to \$61 billion in 1996-99. MA purchases by firms from developing countries rose from an average of \$8 billion in 1991-95 to \$30 billion in 1996-99.

In varied attempts to reduce costs and improve profitability, most major South African banks are examining possibilities of merging with insurers or other banks, while many others are expanding into other African countries. Standard Bank (Stanbic) expanded into 14 African countries in the 1990s, believing this would allow it to be the financial services provider for industries wishing to tap African markets. An attempted hostile takeover of Stanbic by Nedcor was blocked by the Minister of Finance in 2000, partly because of competition concerns, fears of increased systemic risks and the possible loss of up to 10,000 jobs in a country with extremely high unemployment. In arguing its case to the regulatory authorities, Nedcor advanced the need for South Africa to have a "national champion" to compete on a global scale. It claimed the merger would result in enhanced revenues, risk mitigation and cost reduction. These arguments were disputed by Stanbic that highlighted the failure of similar mergers elsewhere and noted that 70-80 percent of mergers in financial services did not deliver the efficiency touted. Among the reasons it stressed for merger failures were the loss of talented staff, low employee morale, unrealistic estimates of synergy benefits, under estimation of revenue losses and unexpected difficulties in integrating back office functions and systems.

In Ghana, banks like Societe Generale, Eco Bank, Access Bank and United Bank of Africa (UBA) have gone through MA experiences. Societe Generale emerged from a merger of SSB Bank and National Savings and Credit Bank in 1994; Ecobank merged with Trust Bank in 2000; Access Bank merged with Inter-continental Bank in 2011; and UBA merged with Amalgamated Bank in 2012. Most of the synergies in support of MA appeared to have been positively considered in going through the MA experiences in all the above examples in Ghana.

DATA AND ORGANIZATION

Data Types

The main data for the study is secondary and the sources include official publications of Societe Generale, the Bank of Ghana (BoG), Ghana Stock Exchange (GSE), and other relevant local banking institutions with respect to their Annual reports and Financial statements of several years, spanning pre- and post merger periods (1994 up to 2004). These sources will enable extraction of relevant financial information and information on operational efficiency. The internet will be used to extract relevant data to supplement the secondary data source. Discussions with some selected senior officials of the bank will be entered into so as to iron out likely inconsistencies that may come up. Information gathered will be processed and analysed using Microsoft Excel package.

Data Organization

The method will look at such criteria of profitability (Antwi-Asare and Addison, 2000) as Return on Assets before tax (RoA); Earnings per share (EPS); and Dividends per share (DPS) in the pre-merger and post-merger periods. Indicators of operational efficiency including varied efficiency ratios will be considered such as: Expenses to total assets (E/TA); Provisions for Bad Debt/Total Assets (PBD/TA); Net Loan Loss Provisions/Total Assets or Total Loans (NLP/TA); also in the pre-merger and post-merger periods. The year 1994 will be considered as the pre-merger year; and two specific periods in be post-merger periods: 1999 and 2004; that is, the five-year interval after 1994 to enable us gauge the progress or otherwise of a post-merger period over a decade, using ratios of profitability and operational efficiency, Chi-square and test of statistical significance will be employed to consider the difference, if any, between pre-merger and post merger periods.

Table 1 provides information on the criteria of profitability and operational efficiency in the pre- and post-merger periods and the framework for effective analysis to determine whether or not Societele Generale's merger and acquisition experience has been a blessing. This table may be considered as the framework on which our analysis with

respect to profitability and operational efficiency is based. The criteria and expected signs are as indicated in Table 1.

Table 1. Criteria of profitability and Operational efficiency

I Profitability Criteria (ratios)	Premerger 1994	Post-merger		1999 ----	Post-merger		2004 (Sign)----	Chi-Sq ratio	t-
		Expected ---(Sign)-----	Actual		Expected	Actual			
i Return on Asset (RoA) % before tax		(+)			(+)				
ii Earnings /share (EPS) C.		(+)			(+)				
iii Dividends /share C.		(+)			(+)				
II Operational Efficiency (ratios)									
i Expenses to Total Assets (E/TA)		(-)			(-)				
ii Provision for Bad Debts/ Total Assets (PBD/TA)		(-)			(-)				
iii Net Loan Loss Provision / Total Assets (NLP/TA)		(-)			(-)				

Source: Computed from Societe Generale's Annual Reports and Financial statements of several years (1994-2004)

- I Profitability Criteria:**
- i Return On Asset before tax (ROA) %
 - ii Earnings per share (EPS) GHC
 - iii Dividends per share (DPS) GHC
- II Operational efficiency ratios:**
- i Expenses to Total Assets (E/TA) %
 - ii Provision for Bad Debts to Total Assets (PBD/TA) %
 - iii Net Loan Loss Provision to Total Assets (NLP/TA) %

ANALYSIS OF RESULTS AND DISCUSSION

Table 2. Profitability Criteria (Ratios)

Period	EPS	DPS	Total	Trend Analysis (RoA) %
Pre-merger (1994)	160	60	220	6%
Post-merger (2004)	1500	900	2400	7%
Total	1660	960	2620	
Chi-sq value = 0.87, not statistically significant different at 5% confidence level				
thus over the ten year period, the increase was only a very modest 1%. This value goes to buttress the lack of statistically significant difference at 5% confidence interval given by the chi-sq measure)				

Source: Computed from Societe Generale's Annual Reports and Financial statements of several years (1994-2004)

Analysis of the profitability criteria will be made with reference to Table 2 that provides information on related measures.

Return on Asset (ROA): Profits before tax/Total Assets. It shows how well bank management has used the resources at its disposal to generate additional resources for the bank at the end of the year. Continued positive growth in this measure is required for the viability of any bank. ROA is therefore expected to show a positive sign as indicated in Table 1.

Earnings per share (EPS) Calculated as: (Net Income – Dividends on Preferred shares) /Average outstanding shares, normally at the end of the period. This ratio is generally considered to be the single most important variable in determining the share's price, and also a major component used to calculate the price-to-earnings ratio. An important aspect of EPS often ignored is the capital that is required to generate the earnings (net income) in the calculation. For example, two companies could generate the same EPS ratio, but one could do so with less equity (investment), implying that the one would be more efficient at using its capital to generate income and, other things being equal, would be considered a more efficient company. This matter will be touched on in the next section, when considering the company's operational efficiency analysis.

Dividends per share (DPS) calculated as: $DPS = (D - SD) / S$, where D – sum of Dividends over a period (usually one year); SD - Special, one time dividends; and S – Shares outstanding for the period. Dividends are a form of profit distribution to the shareholder. A growing DPS can be an indication that the company's management believes that the growth can be sustained.

Table 2 illustrates that the three measures of profitability, namely, ROA, EPS and DPS are positive in the post-merger period (2002), but the Chi-Sq value = 0.87, means that the difference appears not to be statistically significant at 5% confidence level, which appears to be only a modest positive financial performance. Using trend analysis in the last column of Table 2 the value for 2004 ten years after the merger was only 7% (but the value in 1994, ten years after the

merger was 6%, an increase of a very modest 1%). This value goes to buttress the lack of statistically significant difference at 5% confidence level given by the chi-sq measure).

Financial ratios may have their own drawbacks in financial profitability analysis, yet they can serve useful purposes in situations of related studies (Salami, 2011).

With the apparent positive values reported in Table 2 for all the three criteria of profitability, this study is able to confirm the position of past researchers like Panetta et al. (2003), Boot (2003), Amel et al. (2004), and Al-Shankes et al. (2007) who contend that MA activities can have positive impact on increase in profits in the context of share value maximization, even though researchers like Caruso and Palmucci (2008), and Piloff and Santomero (1998) hold contrary views. But we should remember that the results of our current study appear not to be statistically significant at 5% confidence level as far as financial performance is concerned.

Analysis of operational efficiency will be done with respect to Table 3 which provides relevant ratios in the post- and pre-merger years. The ratios are:

i Expenses to Total Assets Ratio (E/TA): it is a measure of a company's cost of operation as a percentage of its total assets. This measure appears to constitute the most important single cost or expense factor that determines the operational efficiency of the company, and all other measures in this section tend to be affected by it. All potential benefits conferred by economies of scale seem to derive from this measure. The size and direction of the other ratios go to affect the Expenses to Total Assets ratio. These expenses consist primarily of management fees and additional expenses such as trading fees, legal fees, auditor fees and other operational costs. The size of the ratio is important to investors as it affects investors' returns

ii Provision for Bad Debts to Total Assets Ratio (PBD/TA): It is a financial ratio that indicates the percentage of a company's assets provided in debt. An efficient company should always be able to institute or put in place control measures so as to reduce the volume and therefore the ratio. The ratio is expected to be negative (-) as indicated in Table 1.

iii Net Loan Loss Provision to Total Assets Ratio (NLP/TA): It is meant to cover estimated losses on loans due to defaults and non-repayment. Its significance is that it indicates to a bank how stable is its lending base. A reduction in the size of this ratio is always the case in theory. But increase in loan loss may not necessarily be due to bad lending decisions; changes in macro-economic factors, for example, could hit responsible borrower hard.

The figures in Table 1 must in theory be negative, but the actual figures shown in Table 3 do not appear to indicate any cost reduction or increase in operational efficiency. The related Chi- Sq. value is 0.33 (statistically significant at 5% confidence level. For example, E/TA ratio in 1994 was 5%, while the post-merger figure for 2004 was up to 9%. Other figures in the table have also not shown any appreciable decrease, which seem contrary to the opinion of researchers like Rhoades (1998), Al-Sharkas et al. (2007), Forcarelli and Paretta (2003) and Vennet (1996) who have reported increase in operational efficiency and cost reduction. But their stand is contrasted by Peristiani (1997) and Saibu (2013) who have reported lack of cost reduction and operational efficiency. Nevertheless, Peristiani in his review of the generality of explanations appears to support continued merger activity. Saibu reports of increases in costs of security, power generation, and even social infrastructure like roads, water, etc all of which add up to produce a huge total expenses bill. In our earlier section, positive financial performance improvement was reported contrary to lack of cost reduction and operational efficiency. This may imply that an organization could pass the test with respect to profitability, but go down with respect to cost reduction and operational efficiency. This reasoning seems to explain the relevance of structure-conduct-performance paradigm that confirms existence of profits in the face of reduction in cost and operational efficiency.

Table 3. Operational Efficiency criteria (Ratios)

Periods	E/TA	PBD/TA	NLP/TA	Total
Pre-merger (1994)	5	3	N/A	8
Post merger(2004)	9	3	N/A	12
Total	14	6	N/A	20

(The chi-sq value is 0.33 which is statistically significant at 5%) confidence level

Source: Computed from Societe Generale's Annual Reports and Financial Statements of several years (1994-2004)

Table 4. Comparison of profitability and operational efficiency of Societe Generale and banking industry average (2004)

Criteria	Societe Generale	Banking industry average
Total Expenses (Ghc m)	100,055,063	81,921,210
Charge for Bad debts (Ghc m)	22,019	23,712
Interest Expense (Ghc m)	71,416	58,394
Interest Income (Ghc m)	245,731	422,246 (average for the 4 big banks: GCB; BBG; SCG & Societe Generale)

Source: computed from BoG annual reports of the banking industry

Table 4 provides some information on comparison of some criteria between Societe General and the banking industry average. Such a comparison could help us gauge information on financial performance and cost efficiency of Societe Generale with the banking industry average. For example, the figure for Total Expenses for the bank in 2004 was Ghc. million 100,053,003, compared with the banking industry average of Ghc. million 81, 921,210, a clear difference of Ghc. million 18, 133,853. This goes to buttress our earlier stand on Societe Generale being characterized by relatively higher costs and expenses, and therefore lower operational efficiency. Societe Generale's figures on interest expenses appear much higher than the banking industry average, even though the industry average for interest income of Ghc million 422, 246 was much higher than that of Societe Generale of Ghc. million 245, 731. The implication of these figures is that Societe Generale appears to be a relatively higher cost and less efficient company as compared to its banking industry average. It thus behoves on the bank to step up all efforts to improve operational efficiency through comprehensive and drastic costs reduction to realize the benefits of economies of scale.

CONCLUSIONS AND RECOMMENDATIONS

A number of conclusions have resulted from this study. Firstly, Societe Generale that has pioneered the evolution of mergers and acquisitions in Ghana's banking industry has valuable experiences which can be of tremendous benefit to the entire Ghana's banking industry. Secondly, the bank has made only modest positive improvements in the area of financial performance, even though the difference between the pre-merger and post-merger periods cannot be said to be statistically significant at 5% confidence level. Besides, the bank has experienced some challenges with respect to cost and operational efficiency. Varied expenses and other operational costs have posed a limitation to the bank's effort to achieve costs reduction and positive operational efficiency. Our study has revealed that the bank has experienced much higher costs and expenses, indicating less operational efficiency as compared to the average of its banking industry.

Following from above, the study makes the recommendation that the bank initiates a study that will investigate the factors that are responsible for the apparent excessive costs and expenses, possibly using a regression method. Secondly, the bank should be able to identify and promote specific areas that constitute candidates for improved income generation and reduction in corresponding expenses both of which will help to maximize the earnings potential of the bank. Moreover, the government should be able to create or promote the enabling environment, for example, that concerns infrastructure provision, as a way of achieving cost reduction that could motivate similar institutions in Ghana.

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