IMPACT OF MERGER AND ACQUISITION ON OPERATING PERFORMANCE AND SHAREHOLDER WEALTH IN PAKISTAN BANKING SECTOR.

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ABSTRACT
In the present paper we investigated the impact of Merger and Acquisitions on operating performance and shareholder wealth in Pakistani banking sector. Paper studied the impact on acquiring firms before and after the transaction. We have selected 3 transactions of merger and acquisitions in Pakistani banking sector from 2007 to 2010 with both domestic and foreign banks which are operating in Pakistan. We have used event study methodology to determine the post merger impact on operating performance and shareholders wealth of the bidder firms. The present study showed that after the transaction the operating performance from the figures that the ratios of operating performance has decreased significantly which shows that the transaction doesn’t have a positive relationship with the operating performance of the banks. As the shareholder’s wealth is considered study showed from the tables that the earning per share of all the three banks have decreased significantly after the transaction which shows that there is a negative effect of merger and acquisition transaction on the earning per share or shareholder wealth. Hence the null hypothesis is accepted.

KEYWORDS: Merger, Acquisition, Operating performance, Share Holder wealth
INTRODUCTION
Merger and Acquisition was once a US business phenomenon but during the fifth merger and acquisition wave it spread all over the world. Now the merger and acquisition is also used in developing economies especially in Asia. The paper will investigate the impact of merger and acquisition on operating performance and shareholder wealth. “The operating performance of a firm is the measure of profitability in relation to sales revenue”. “The shareholder’s wealth is defined as the present value of expected future returns to the owners i.e. shareholders of firm. The operating performance is measured by three dimensions that are operating profit margin, gross operating margin and net profit margin, and we will measure the shareholder wealth by using earning per share (EPS).

In any country the commercial banks are the backbone of that country. A well established banking system is very necessary for the economic stability of a country. Commercial banks meet the financial needs of various sectors of economy. For the development of a country it is very necessary that it has a well established banking system. Banks play an important role in economic development of a country. Pakistan has a well established banking system. Banking is an important factor of Pakistan economy. The banking sector has flourished in past and a number of local as well as foreign banks have opened their branches in Pakistan. In Pakistan banking sector merger and acquisitions transactions has occurred in last 20 years. In Pakistan merger and acquisition is not a common business phenomena due to which the volume of merger and acquisition transactions is very low. The banking sector of Pakistan is the sector where most of the merger and acquisitions transactions have occurred.

PROBLEM STATEMENT
Impact of merger and acquisition on operating performance and shareholder wealth in Pakistan banking sector.

RESEARCH OBJECTIVE
  o To see the impact of merger and acquisitions on operating performance of firm in Pakistan banking sector.
  o To see impact of merger and acquisitions on shareholder wealth in Pakistan banking sector.
  o To provide a better understanding of merger and acquisition transactions.

RESEARCH QUESTIONS
  o Whether the operating performance of bidder firms is affected after merger and acquisition.
  o Whether the shareholders wealth is affected after merger and acquisition in Pakistani banking sector.
SIGNIFICANCE OF THE STUDY

Banking sector is bone of Pakistani economy and research on this sector is very important to improve the overall performance of this sector. This sector is more active sector in Pakistan that’s why the mergers in this sector will definitely affect the whole economy of Pakistan. Our study will provide this sector to take decisions about mergers and acquisition. It will help to take decisions regarding the operating performance and shareholders wealth. It will also helpful in making merger and acquisition decisions by keeping in view the operating performance and shareholders wealth. Our study will be helpful for new researchers and students to get familiarity with the basic principles of mergers and acquisition.

LIMITATIONS OF THE STUDY

The sample size is small. Generalizibility of the research is less due to small sample size. It only covers the banking sector; its results cannot be applied on other business sectors. The period which we are considering in our research was the period during which there was recession due to which it can also affect the shareholder wealth and operating performance of the firm.

LITERATURE REVIEW

Trivedi et al. (2013) studied the operating performance and shareholder value of acquiring companies and comparing their performance before and after the merger in Indian oil and gas sector. They concluded that mergers do not improve financial performance at least in short term. Sana & Nishat investigated the short term market response associated with seven Merger and Acquisition in banking sector of Pakistan. They divided the merger and acquisition transactions in three categories. Their results indicate statistically significant investor reactions around the merger announcements. The combined mean CARs for the target banks group and bidder group are both positive and statistically significant.

Ma, et al. (2009) examined the abnormal return to 10 Asian stock markets. They selected a total of 1477 Merger and Acquisition transactions in 10 Asian stock markets. They used the event study methodology to measure the abnormal return before and after the transactions in three event windows they found that stock markets has positive cumulative abnormal returns in three different event windows. The findings suggest that the financial benefits related with merger and acquisition deals are beneficial and it is helpful in external growth of firms so it is highly recommended to mangers. Saxena & Rawat, (2007) observed the pre merger and post merger performance of Indian aluminum industry by using different profitability measures. Data of some selected companies was collected from secondary sources and financial statements of the
companies. The results showed that mergers and acquisition do not improve the efficiency, profitability and accelerated growth of the companies after the merger transaction.

Mantravadi & Reddy explored the impact of mergers on operating performance of acquiring corporations of various industries. They examined the pre merger and post merger financial ratios of sample companies including public and private companies in India. The period of investigation was from 1993 to 2003. The results showed that companies of banking, Textile and pharmaceutical sectors have improved operating performance after mergers but other sectors like chemicals and agricultural sectors decline after mergers.

THEORETICAL FRAMEWORK

HYPOTHESIS

\(H_0\): There is no positive relationship between Merger and Acquisition and operating performance and shareholder’s wealth.

\(H_1\): There is a positive relationship between Merger and Acquisition and operating performance and shareholder’s wealth.

SAMPLE FOR THE STUDY

We have selected three Pakistani banks which have acquired

- Faisal Bank acquired RBS on June 17, 2010.

METHODOLOGY

In this paper we will use the event study methodology to determine the impact of merger and acquisition on operating performance and shareholder wealth. An event study measures the impact of a specific event on the value of the firm. We will use secondary data for analysis.

DATA AND ANALYSIS

Three ratios are calculated for operating performance and one ratio for shareholder wealth. The operating performance is measure of profitability in relation to the sales revenue, shareholder wealth is what returns a share holder gets against the shares he had held. We
have analyzed that what is the effect on operating performance and shareholders wealth by the help of the tables below. The ratios for NIB bank are in Table #1, Faysal bank Table #2, and Standard Chartered bank Table #3.

<table>
<thead>
<tr>
<th>NIB BANK</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Profit Margin</td>
<td>43.29%</td>
<td>37%</td>
<td>44.88%</td>
</tr>
<tr>
<td>Gross Profit Margin</td>
<td>29.92%</td>
<td>28%</td>
<td>28.95%</td>
</tr>
<tr>
<td>Net Profit Margin</td>
<td>2.74%</td>
<td>-5%</td>
<td>-49.15%</td>
</tr>
<tr>
<td>Earning Per Share(EPS)</td>
<td>0.37</td>
<td>-0.32</td>
<td>-2.63</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>FAYSAL BANK</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Profit Margin</td>
<td>46.01%</td>
<td>49.73%</td>
<td>46.05%</td>
</tr>
<tr>
<td>Gross Profit Margin</td>
<td>29.42%</td>
<td>29.38%</td>
<td>31.93%</td>
</tr>
<tr>
<td>Net Profit Margin</td>
<td>7.08%</td>
<td>6.03%</td>
<td>4.44%</td>
</tr>
<tr>
<td>Earning Per Share(EPS)</td>
<td>1.97</td>
<td>1.45</td>
<td>1.55</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>STANDARD CHARTERD BANK</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Profit Margin</td>
<td>96.28%</td>
<td>98.99%</td>
<td>98.80%</td>
</tr>
<tr>
<td>Gross Profit Margin</td>
<td>70.96%</td>
<td>71.86%</td>
<td>70.44%</td>
</tr>
<tr>
<td>Net Profit Margin</td>
<td>39.19%</td>
<td>12.26%</td>
<td>2.90%</td>
</tr>
<tr>
<td>Earning Per Share(EPS)</td>
<td>3.06</td>
<td>0.71</td>
<td>0.16</td>
</tr>
</tbody>
</table>

RESULTS

Three ratios are calculated for operating performance i.e. operating profit margin, Gross profit margin, net profit margin and one ratio for shareholder wealth i.e. earning per share (EPS) for one year before the transaction the year of transaction and one year after the transaction for three banks. After the transaction the operating performance from the above figures that the ratios of operating performance has decreased significantly which shows that the transaction doesn’t have a positive relationship with the operating performance of the banks. As the shareholder’s wealth is considered we can see from the tables that the earning per share of all the three banks have decreased significantly after the transaction which shows that there is a
negative effect of merger and acquisition transaction on the earning per share or shareholder wealth. Hence the null hypothesis is accepted.

CONCLUSION
In the Pakistani banking sector the merger and acquisition is not good for the operating performance and shareholder’s wealth. Hence we can recommend that it is not beneficial for shareholders as their return on equity is reduced significantly. The merger and acquisition transactions reduced the shareholders wealth significantly in Pakistan banking sector but in this paper the sample size is small with the help of bigger sample size and increasing the time frame after the transaction one can get the better understanding that it should be recommended to the banks or not in Pakistan banking industry.
REFERENCES


