

EXECUTIVE SUMMARY

The impetus to undertake this research project began about 2 years ago when we commenced our MBA programme. We became aware of the challenges facing the domestic banks in their quest to strengthen the banking sector to be better equipped to respond to the new and challenging requirements of the local and global economy. The bank merger exercise was inevitable in the face of globalisation and borderless trade.

The first step towards enhancing efficiency and alleviating the level of competitiveness was the consolidation of the 54 domestic banking institutions into 10 banking groups. There was significant rationalisation of the wide range of common functions and operations across institutions in the banking groups. Ten banking groups are now leveraged on cross-selling of their products and services across institutions in the group.

We were interested in researching the impact the merger exercise had on the various stakeholders - shareholders, bank employees, customers and relevant government bodies. We analysed the financial performance of banks before and after the merger exercise to study the impact on profitability, shareholder funds, share prices, asset size, CAR and PE ratio. We also examined the non-financial consequences of the merger on various stakeholders like employees, shareholders and politicians.

Our analysis also incorporates the accounting methods adopted in the financial reports by the various anchor banks on consolidation with their merger partners. We observed the different accounting treatment of goodwill arising from the merger by the anchor banks.

Our findings revealed that the merger exercise was only successful in reducing the number of commercial banks from 54 to 10 in a short period i.e. from July 1999 to December 2000. From 1980 to 1999 the results were dismal as there was only one reduction in the commercial banking institution when BNM used moral suasion to encourage the reduction in the number of banks in the sector. Apart from reducing the number, the consolidation exercise did not meet the desired goals of achieving synergy in terms of asset quality or shareholder value. There was no significant improvement in terms of quality or price of the services. The ultimate objective of the merger exercise was to create bigger and better managed banks with efficient delivery channels. This is to ensure that local banks do not fizzle out when the financial services sector opens up to foreign challenge. But the pace of the mergers, in some cases like in the UBG is not at the desired rate. Many of the exercises resulted in mergers in face value only, without any drastic reduction in cost or increased efficiency.

The merged entities should have strong shareholder and efficient management team. The events of these past few months from our analysis show that the banking merger mania has not brought about better banks but fewer banks with the same standard of delivery. Our findings also uncover inequitable terms and conditions imposed by the authorities on some banks, as those with political clout had an unfair advantage over other well managed banks.

Our recommendations include further consolidation to eventually have only three banks in the country to enhance the banking sector's capacity to be able to withstand all kinds of pressure from within and outside the country. We propose that future consolidation be market driven with market forces determining the partners and the terms of consolidation with no authority intervention. We wish to suggest that Banks invest in IT to be on par with the foreign banks delivery system. Banks need to undergo a paradigm shift in the way they do business. They may have to reinvent their philosophy from one of mass production to mass customisation; from a general service for all to a one-to-one customer service platform; from a standard delivery channel to multiple delivery channels; from fixed banking hours to flexitime, and from physical contact to a secured wireless environment. Further local banks should adopt business models adopted by banks in developed financial markets by concentrating on their core competencies and out sourcing other services in which they do not have comparative advantage. Unless a bank is prepared to meet all these changes, it may not be in a position to retain customer loyalty which is the backbone of the banking industry.