

## Chapter 3

### Recent Bank Mergers in Malaysia

#### 3.1 Introduction

The Asian crisis in 1997 has been the starting point where Malaysian banks faced major merger exercises. Even on the eve of the Asian Financial Crisis, 1 July 1997, there was seen a bank merger taking place between DCB Bank and Kwong Yik Bank. In its wake, the year before Malaysia experienced its strongest economic growth since the Asian Financial Crisis, Bank Negara Malaysia (BNM) announced a national merger and consolidation programme in the banking sector on 29 July 1999. The wave of these banking mergers saw Malaysia's fifty four financial institutions in 2000 being grouped to ten anchor banks, with the last merger dated March 2003.

However, this was not the first time a crisis had forced some banks to be merged or absorbed. In the mid 80's, the economic recession had force BNM to rescue several financial institutions from insolvency due to overwhelming non performing loans (NPLs). Before the crisis, there were forty seven finance companies and there were only forty left after BNM had acquired shares of several ailing commercial banks while some finance companies were absorbed by stronger ones. However, this scenario is slightly different from the ones being discussed as the threat of going out of business was not an immediate threat to most of the merging parties as it was then (Star Business, 1999).

In this chapter, a brief description of each of the ten anchors banks will be discussed.

### 3.2 Domestic Bank Mergers

Merger and acquisition programme is a key component of the Financial Sector Master plan of BNM as a way for domestic banks to compete in the regional and global financial services market (Global Finance, 2003). Notwithstanding the difficult times, BNM still sees pockets of opportunities in mergers and acquisitions in the banking industry (Malaysia Rating Corporation Berhad, 2000).

The proposed schedule suggested that all the mergers should be completed by 31 March 2000 and the merged entities were to begin operations on the 1 April 2000. The timetable proposed was as follows:

|                   |                                                                    |
|-------------------|--------------------------------------------------------------------|
| 30 September 1999 | Signing of Memorandum Of Understanding                             |
| 15 November 1999  | Completion of Due Diligence <sup>1</sup>                           |
| 31 December 1999  | Signing of Sale & Purchase                                         |
| 28 February 2000  | Obtaining approvals from the relevant authorities and shareholders |
| 31 March 2000     | Vesting Order <sup>2</sup>                                         |
| 1 April 2000      | Begin operations as new merged entities                            |

Source: Budget 2000, November 1999

In the original plan, BNM named six "anchor banks": Maybank Berhad, Bumiputra-Commerce Bank Berhad, Public Bank Berhad, Perwira Affin Bank Berhad, Multi Purpose Bank Berhad and Southern Bank Berhad in 1999 (Bank Negara Malaysia, 1999).

<sup>1</sup> An assessment of the viability of the merger/acquisition as an ongoing concern

<sup>2</sup> Vesting Orders are court approval to effect the transfer of the merged banking business

Unfortunately, it was noted that not all parties were willing to abide by the original plan. As a result, in October 1999, The National Economic Action Council (NEAC) chaired by Dato' Seri Dr Mahathir Mohamed admitted that the earlier proposal "was causing too many ripples and this was not good for the economy" and hence announced that until and unless the banks are ready, they shall not be forced to merge (National Economic Action Council, 1999).

BNM had been more flexible in considering all proposals of the anchor banks and their respective partners and the completion date for bank mergers. In February 2000, BNM announced that the accepted "anchor banks" now stood at ten, in addition to the six original "anchor banks", the four new players were RHB Bank Berhad, AmBank Berhad, Hong Leong Bank Berhad and EON Bank Berhad. To ensure the banking institutions (BIs) are well capitalised, the Central Bank had imposed the dateline of 31 December 2001 for the banking sector to increase capital to the minimum requirement of RM2 billion each for the domestic proposed banking groups.

However, a new target date of 31 December 2000 was set, implying a delay of six months from the initial plan, for the completion of the entire merger and consolidation exercise. In retrospect, this was in fact too ambitious to achieve as the last domestic bank merger, which was between Bank Utama Berhad and RHB Bank Berhad was only completed in March 2003.

Upon completion of the merger programme among domestic BIs, the number of domestic BIs has been significantly reduced to ten anchor banks. The ten anchor banks are Malayan Banking Berhad, Bumiputra-Commerce Bank Berhad, RHB Bank Berhad, Public Bank Berhad, Arab-Malaysian Bank Berhad, Hong Leong Bank Berhad, Perwira Affin Bank Berhad, Multi-Purpose Bank Berhad, Southern Bank Berhad and EON Bank Berhad, as shown in the Table 3.1:

**Table 3.1: The Ten Anchor Banks in Malaysia as of January 2005**

| <b>Commercial Banks</b>               | <b>Short History on Merger</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|---------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Affin Bank Berhad</b>              | Established 23 October 1975 as Perwira Habib Bank Malaysia Berhad. On 26 April 1994 its name changed to Perwira Affin Bank Berhad. On 1 January 2001 BSN Commercial Bank (Malaysia) Berhad merged with Perwira Affin Bank Berhad to become Affin Bank Berhad                                                                                                                                                                                                                                                                                                                                                                                              |
| <b>Alliance Bank Malaysia Berhad</b>  | Established 31 August 1982 as Malaysian French Bank Berhad. The bank was established to take over the business of the Kuala Lumpur Branch of Banque Indosuez. The Kuala Lumpur Branch of Banque Indosuez had been in operations since 1958. On 2 April 1996 the name of the bank was changed to Multi-Purpose Bank Berhad. Multi-Purpose Bank successfully completed the merger exercise on 1 January 2001 with International Bank Malaysia, Sabah Bank, Sabah Finance, Bolton Finance, Amanah Merchant Bank and Bumiputera Merchant Bankers. It changed its name to Alliance Bank Malaysia Berhad and its corporate logo was launched on 19 January 2001 |
| <b>AmBank Berhad</b>                  | Established on 1 August 1994 as Arab Malaysia Bank Berhad and later changed to AmBank Berhad on 15 June 2002. Part of its group includes MBF Finance Berhad which was merged into the group in 2001                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| <b>Bumiputra-Commerce Bank Berhad</b> | Established in 30 December 1972 as United Asian Bank Berhad. On 31 October 1991 the operations of Bank of Commerce Berhad and United Asian Bank Berhad were merged                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |

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|--------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Bumiputra-Commerce Bank Berhad (continue)</b> | to form the Bank of Commerce (M) Berhad. On 1 October 1999 Bank Bumiputra Malaysia Berhad merged with the Bank of Commerce (M) Berhad and had its name changed to Bumiputra-Commerce Bank Berhad                                                                                                                                                                                                             |
| <b>EON Bank Berhad</b>                           | Established on 4 November 1963 as Kong Ming Bank Berhad. On 2 September 1992 the name of the bank changed to EON Bank Berhad, as a result of a substantial share equity acquisition by Edaran Otomobil Nasional Berhad (EON). On 1 January 2001 Oriental Bank Berhad merged into EON Bank Berhad                                                                                                             |
| <b>Malayan Banking Berhad</b>                    | Established 12 September 1960 as Malayan Banking Limited Company. On 5 April 1966 the name of the bank changed as Malayan Banking Berhad. On 1 January 2001 the banking business of The Pacific Bank Berhad was acquired by Malayan Banking Berhad. On 1 March 2001 PhileoAllied Bank (Malaysia) Berhad merged into Malayan Banking Berhad                                                                   |
| <b>Public Bank</b>                               | Incorporated in Malaysia on 30 December 1965 and commenced business on 6 August 1966. On 31 March 2001 the Bank completed its acquisition and merger of the commercial banking business of the former Hock Hua Bank Berhad                                                                                                                                                                                   |
| <b>RHB Bank Berhad</b>                           | Established on 4 October 1965. RHB Bank Berhad has gone through 3 mergers. The first merger was between DCB Bank Berhad and Kwong Yik Berhad on 7 July 1997. On 1 July 1998 RHB Finance was absorbed by RHB Bank Berhad. On 30 June 1999 the banking business of Sime Bank Berhad was acquired by RHB Bank Berhad. In October 2000, RHB Bank Berhad acquired two finance companies, Delta Finance Berhad and |

|                                       |                                                                                                                                                                                                                                                                                |
|---------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>RHB Bank Berhad<br/>(continue)</b> | Interfinance Berhad. On 1 May 2003 Bank Utama (Malaysia) merged with RHB Bank Berhad. Its major shareholders are Utama Banking Group Berhad and The Employer Provident Fund                                                                                                    |
| <b>Southern Bank Berhad</b>           | Incorporated in 21 December 1963 as Southern Banking Limited. In 1964 its name changed to Southern Banking Berhad and later in 1984 was changed to Southern Bank Berhad. On 27 April 2000 the banking business of Ban Hin Lee Bank Berhad was acquired by Southern Bank Berhad |

Source: The Bankers' Almanac, January 2005

As of 31 March 2001, the domestic BIs controlled about 75 per cent of banking sector's market share, in terms of total assets and total deposits. Despite the dominance of the domestic BIs, the fourteen fully foreign-owned BIs have made a strong presence in the domestic banking sector (BNM, 2001).

In order to become more competitive, the logical solution is to automatically reduce the number of local BIs in Malaysia. However, BNM is adopting a more reasonable approach to ensure that the merger exercise would not in any means disrupt the normal operations of the BIs, which is a guided merger (BNM, 1999). This involves BNM taking a more proactive role in solving issues involved with the principle of fairness being applied to all parties of a merger – not by forcing of closure similar to some International Monetary Fund (IMF) guided countries like South Korea. In the meantime, all BIs are reminded to continue pay emphasis on loan growth, which is a vital ingredient in the recovery process of the economy. Besides playing a mediator role should the need arise, BNM has and is continuing to take steps towards making merged banks more competitive and more efficient in order to compete with foreign banks. At a recent keynote address at the Dialogue Session with Banking Institutions, Governor Tan Sri Dato' Sri Dr. Zeti Akhtar

Aziz spoke of BNM's contribution to the mergers. She mentioned about the two important infrastructures put in place by BNM, firstly the framework for the establishment of Islamic subsidiaries, and secondly, the merger of commercial banks and finance companies within the same banking groups. These frameworks are just some of the things BNM have implemented to increase BIs efficiency and ultimately, competitiveness (Bank for International Settlements Review, 2005).

In order to ensure that the consolidation programme is implemented within the stipulated timeframe, without affecting the value of the merged, minimum disruption in banking services during this ongoing merger exercise, the involvement of BNM indeed served as a catalyst to spur the consolidation programme. Evidence of this was apparent from the start as BNM announced that it would directly select the merger partners to ensure that the merger objectives are met, should shareholders of BIs do not make use of its freedom to do so.

The Government had extended the following tax benefits for the merger programme to minimise the post-integration costs (BNM, 1999).

- (i) Exemption of stamp duty and real property gains tax that was announced in the 1999 Budget had been extended to 30 June 2000; and
- (ii) Recognition of 50 per cent of the accumulated losses of BIs that are to be acquired for the purposes of computing the tax payable by the merged entity through tax credit. The credit must be utilised within two years from the completion of the merger exercise.

Apparently, these tax incentives would result in substantial revenue losses incurred by Government. However, with the continuing deregulation and globalisation in the

financial services sector and as the importance of the merger exercise can be foreseen, the Government is willing to forego such revenue in order to ensure that the cost of the merger can be minimised. With this, the value of the merged entity can be enhanced and a more efficient banking group can be created to survive in an increasingly intense competition. Evidence of this can be seen even as recent as 2004 when the Return On Assets (ROA) of top domestic banks was higher than foreign banks at 2.4 per cent. Top domestic banks also managed to control costs better and have closed the gap on foreign banks as far as productivity and asset quality are concerned. At the end of 2004, domestic BIs still control 76 per cent of the banking system's total assets and 78.9 per cent of gross loans (AsiaViews, 2005).

However, it is not all a bed of roses as costs for mergers can be expensive resulting in a drop in earnings, although it may not result in losses for the financial year. For example, AMFinance Berhad's (AmFinance) profitability dipped in FYE 31 March 2002 (FY 2002) (pre-merger) and 1Q FY 2003 (post-merger), mainly due to one-off merger-related costs. Nevertheless, the streamlining of its backroom activities as well as contributions from the merger are expected to boost its future profits, that are expected to be visible by FY 2004. However, after the merger, despite the drop in profitability, Rating Agency Malaysia (RAM) has upgraded AmFinance's long-term rating from A3 to A2 and reaffirmed its short-term rating at P1. For most of the mergers of BIs, the one-time cost of mergers will most likely be present but if done prudently and effectively, it can increase the local BIs strength in many areas resulting in better future profits (RAM, 2002).

The merger process has been a market driven process with the close supervision by BNM. As such, the decision to enter into merger negotiations and other decisions relating to pricing and terms of the merger are all determined entirely by the negotiating parties. Deadlines imposed by negotiating partners should therefore not be attributed to BNM. As a result of the consolidation that has taken place in the Malaysian banking sector, ten



anchor banks have emerged, having complied with all the requirements of anchor bank status which include minimum capitalisation, total asset size and other prudential requirements. This achievement has increased the potential of the banking sector to support the changing needs of our economy and to face the increasing challenges of the environment in which we are operating (BNM, 2000).

Anchor bank that will now emerge stronger after the merger, with tremendous improvement in performance either in terms of profitability or cost efficiency is Public Bank Berhad.

The consolidation of the industry will not seriously threaten Maybank's position as the leading bank but actually further increase the group's market share. Maybank, which is merging with medium-size PhileoAllied Bank Berhad, Mayban Finance Berhad, Aseambankers Malaysia Berhad, Pacific Bank Berhad, Kewangan Bersatu Berhad and Sime Finance Berhad, is also arguably the most regional of Malaysian banks, as evidenced by the geographical spread of its operations and their contribution to group profits (up to 30 per cent of its income is derived from Singapore and overseas operations).

Public Bank Berhad, which is fast shedding its reputation as a docile and passive player in terms of lending, still maintains prudent and conservative credit approval and loss provisioning policies. Its share of the domestic banking system is set to expand further with the proposed acquisition of Hock Hua Bank Berhad, which will also provide it with the much needed exposure to East Malaysia. Hock Hua Bank is a small but well managed commercial bank in Sarawak. Public Bank is also merging with Advance Finance Berhad and Sime Merchant Bankers Berhad and together both these acquisitions are expected to complement Public Bank's existing predominantly Peninsular Malaysia operations as

well as fill the current gap in merchant banking. Also in the group is Public Finance Berhad.

Rashid Hussain Berhad executive chairman Abdul Rashid Hussain said he was grateful that Bank Negara has approved RHB Bank as one of the ten banking groups in Malaysia. "We are very honored that we have been given the opportunity to continue to play a lead role in support of the government's consolidation of the financial services industry," he said. RHB Bank is the anchor bank for RHB Sakura Merchant Bankers Berhad, DeltaFinance Berhad and Interfinance Berhad (Asia Times, 16 Feb 2000).

### **3.3 Conclusion**

Under an uncertain, increasingly globalised and extensively liberalised economy, the merger and acquisition strategy adopted by BNM in the banking sector is expected to strengthen our economy. This eventually allows Malaysia to deal with any change in a manner that is in the best interest of Malaysia and to become leaders, at least domestically, so as to compete meaningfully with the foreign banks.

In the next chapter, we discuss the methodology used to test whether domestic bank mergers have increased performance of the ten anchor banks.