CHAPTER 1: INTRODUCTION

1.0 AN OVERVIEW INTO M&A

Mergers and Acquisitions (M&A) is one of the very popular ways among corporates to survive in the 21st centuries and also a very important strategic move to stay competitive in its market. M&A is the combination of two business entities to become one legal entity. Merger usually means merging together on equal basis, and acquisition usually means a larger company acquiring a smaller company. In corporate world, the term merger or acquisition are used interchangeably and commonly known as mergers and acquisitions (Ravichandran, 2009).

Most M&A happens because one particular company felt that it is more efficient to be engaged in inorganic growth either for the purposes of capturing bigger market shares, improving asset qualities, strengthening bargaining power, acquiring best technologies and talents in the market, venturing into different industries, and many more other strategic reasons.

Few of the high profile M&As in the past two decades involving large corporates with well-known branding were AOL and Time Warner, Glaxo Wellcome and SmithKline Beecham, Royal Dutch Petroleum Company and Shell, Exxon and Mobil, Vodafone and Mannesmann, Pfizer and Warner-Lambert, etc.

Malaysia is one the leading developing country and economic body in South East Asia region especially in Association of Southeast Asian Nations (ASEAN). Rich with natural resources coupled with highly skilled labour at relatively lower pay scale, located at a strategic geographical location in Asia Pacific with relatively stable political condition, Malaysia is one of the country actively involved in export and import trading. According to ASEAN trade statistics as of year 2010, Malaysia ranked number three in ASEAN trading volume with USD363.5millions, whereas Singapore and Thailand were ranked one and two respectively with trading volume of USD699.3millions and USD385.0millions. Malaysia's trade ranges from raw agricultural and mining material, semi processed goods and fully manufactured items. Hence Malaysian companies are not only looking to grow its business locally but also in ASEAN or internationally. Malaysian companies, prior to venturing overseas also looking into M&A if they were to strengthen their foothold in Malaysia before competing internationally with other huge company globally. One of the most well-known heavyweight M&A in Malaysia was the merger of Sime Darby, Kumpulan Guthrie Berhad and Golden Hope creating one of the world's leading listed oil palm plantation group.

1.1 BRIEF HISTORY OF MALAYSIAN BANKS M&A

Bank plays a very important role in facilitating and financing all kinds of economic and business activities in Malaysia, either for local or international business transactions and activities. A robust and strong banking system is very important and it is well governed under the supervision of Bank Negara Malaysia (BNM).

M&As in Malaysian bank is not a recent event, it started as early as 1932 in the then Tanah Melayu (Shanmugam, 2003). In 1932, Oversea Chinese

Banking Corporation (OCBC) was formed with the merger of Ho Hong Bank, The Chinese Commercial Bank and Oversea Chinese Bank. During 1960s, Hong Kong and Shanghai Bank (HSBC) acquired Mercantile Bank, meanwhile Chartered Bank acquired Eastern Bank.

The recent waves of mergers and acquisitions in Malaysian banks tracked back to the 1980's, where it was mooted by BNM due to economic recession. The pace and process of M&A happened during the 80's were mainly market force driven, and the banking consolidation that BNM expected did not happened as per expected.

Although many weak commercial bank and finance companies fell into insolvency and financial distress during the 80's economic recession, most of the bank shareholders were more interested of protecting their interest rather than the national consideration (BNM Statement, 1999). Table 1 shows the result of banking consolidation from 1980 to 1999.

Banks	**1980**	**1990**	**1997**	**1999**
Commercial banks :				
- Domestic	21	22	22	21
- Foreign	17	16	13	13
Finance Companies	47	45	39	25
Merchant Banks	12	12	12	12
TOTAL	**97**	**95**	**86**	**71**

Table 1 : Number banks from 1980 to 1999 (BNM Statement, 1999)

During the 1997 Asian Financial Crisis, a lot of Malaysian domestic small banks and financial institutions became vulnerable and unable to maintain high level of capital requirement in order to survive. Nonetheless, most of the economic activities and financing in Malaysia were facilitated by banking industries, hence, the risk would be much concentrated in banking industry when economic goes into a down turn and all other industries funded by the bank is not doing well. Anyway, the government cannot afford to have Malaysian banking industry collapse. Therefore, mergers and consolidations of banks was the step taken by the government to strengthen the banking industry.

Besides, the incoming globalization and liberalization waves in the financial institutions scene throughout the world especially ASEAN, is creating a tougher environment for banking business competition. Financial institutions has got to position themselves in a stronger position to not only adapt themselves to the fast changing economic landscape of the world, but most importantly to survive, as many of the smaller financial institutions in Malaysia are vulnerable to the competitive liberal banking business market.

Foreign banks are still operating in Malaysia with some barriers, hence they are not fully maximizing their advantage to wrestle with Malaysian banks in Malaysia yet. As BNM policies restricts foreign bank from operating liberally in Malaysia, such as very limited branches are allowed to be opened. Once BNM gradually grants more liberal rooms for foreign players in Malaysia, these domestic financial institutions can be easily out-played by the foreign banks.

> *"Pair-ups are necessary for the banks to survive, as next year, in order to fulfil World Trade Organization commitments, Malaysia will permit the foreign banks operating in the country, such as Citigroup and HSBC, to set up as many as four additional branches each."*
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> *(Finance Asia, 16 March 2006)*

In order to prepare Malaysian banks for all these challenges, radical changes happened in banking industry where new policies were introduced by Bank Negara Malaysia (BNM) and Securities Commissions (SC) to drive Malaysian bank's M&A post 1997 crisis. There were two very important development plans executed after the post-Asian financial crisis, the Capital Markets Master Plan (CMMP) and Financial Sector Master Plan (FSMP) respectively in year 2001.

> *"FSMP sets out a ten year plan to develop a more resilient, competitive and dynamic financial system with better practices, that supports and contributes positively to the growth of the economy throughout the economic cycle and has a core of strong and forward looking domestic financial institutions that are more technology driven and ready to face the challenges of liberalisation and globalisation'. The development of domestic institutions that form the core of an efficient, effective and stable financial sector is an important part of this process".*
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> *(Bank Negara Malaysia, 2001)*

> *"Market institutions in Malaysia need to be able to adapt promptly and appropriately to external competitive pressures, as well as to the changing needs and demands of their customers. This means that their business models must be fully aligned with the evolving financial landscape. More fundamentally, they must provide investors with a liquid, efficient, secure and transparent trading environment at competitive costs. This will require appropriate restructuring to tap economies of scale, strengthening the integrity of the market by raising the standards of corporate disclosure."*
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> *(Securities Commission, 2001)*

There were about fifty financial institutions in Malaysia after the crisis, and BNM has decided to force them to merge into 6 major banking groups in July 1999, generally comprising a combination of commercial bank, finance company and merchant bank in each of the banking group. After negotiations from various stakeholders with BNM, BNM with government have announced a program to merge them into ten anchor banking groups in February 2001 (BNM Annual Report, 2001).

The final merger that happened under the plan was between RHB Bank and Bank Utama, on March 2002. The completion of RHB Bank and Bank Utama merger has put down a new milestone in Malaysia banking industry, by BNM successfully consolidating Malaysian domestic banking and be prepared to move on to the new millennium era or liberal and globalised challenging banking environment. The ten anchor banks that were formed are Alliance Bank, Ambank, Bumiputra-Commerce Bank, EON Bank, Hong Leong Bank, Maybank, Perwira Affin Bank, Public Bank, RHB Bank and Southern Bank. The list of anchor banks and the merged entities is shown in table 2.

There were several rounds of rumour and also M&A negotiations that happened between Malaysian banks until end of the year 2011 post BNM driven FSMP M&A, the two most recent done deal M&A in Malaysian banking were Bumiputra-Commerce Bank Berhad (BCBB) with Southern Bank Berhad (SBB) in year 2005, and Hong Leong Bank Berhad (HLBB) with EON Bank Berhad (EON) in year 2011, further consolidating Malaysian banks to eight major banking groups.

Compared to the banking M&As in the 80's and late 90's which are mainly mooted and driven by BNM, banking M&As that happened post FSMP 2001 are not forced merger nor it was mooted by BNM. This applies to the case of M&A for HLBB with EON, and BCBB with SBB.

Acquirers	Banking Institutions in the Group	
	Subsidiaries	**Targets**
Alliance Bank Malaysia Bhd		Sabah Bank Berhad International Bank Malaysia Bhd Bolton Finance Bhd Sabah Finance Bhd Bumiputra Merchant Bankers Bhd
Ambank (M) Bhd	Arab-Malaysian Finance Bhd	MBF Finance Bhd
Bumiputra-Commerce Bank Bhd	Bumiputra-Commerce Finance Bhd	Commerce International Merchant Bankers Bhd Bank Bumiputra
EON Bank Bhd	EON Finance Bhd	Oriental Bank Bhd City Finance Bhd Perkasa Finance Bhd Malaysian International Merchant Bankers Bhd
Hong Leong Bank Bhd	Hong Leong Finance Bhd	Wah Tat Bank Bhd Credit Corporation (Malaysia) Bhd
Malayan Banking Group	Mayban Finance Bhd Aseambankers Malaysia Bhd	PhileoAllied Bank Bhd The Pacific Bank Bhd Sime Finance Bhd Kewangan Bersatu Bhd
Perwira Affin Bank Bhd	Affin Finance Bhd Perwira Affin Merchant Bank Bhd	BSN Commercial Bank Bhd BSN Finance Bhd Asia Commercial Finance Bhd BSN Merchant Bank Bhd
Public Bank Bhd	Public Finance Bhd	Hock Hua Bank Bhd Advance Finance Bhd Sime Merchant Bankers Bhd
RHB Bank Bhd	RHB Sakura Merchant Bankers Bhd	Bank Utama (M) Bhd Delta Finance Bhd Interfinance Bhd
Southern Bank Bhd	Southern Finance Company Bhd Southern Investment Bank Bhd	Ban Hin Lee Bank Bhd Cempaka Finance Bhd Perdana Finance Bhd United Merchant Finance Bhd Perdana Merchant Bankers Bhd

Table 2 : List of Anchor Banks Post Financial Sector Master Plan

The Hong Leong Bank and EON Bank merger will always be remembered as the longest ever banking takeover in Malaysia banking sector. It all started in year 2010, and it took over fifteen month to successfully complete the deal.

There were feuding shareholders and power wrestling in the EON Bank boardrooms resulted from the offer from Hong Leong.

The EON's Hong Kong based shareholder, Primus Pacific Partners, even filed a lawsuit against EON directors, attempting to prevent the takeover after it had paid all the premium prices to acquire EON shares not too long ago, resulting Primus with a hefty lost if the deal went through.

The persistent Hong Leong, with his owner Mr.Quek Leng Chan, had successfully concluded the deal in Mid-2011 by revising its offer price and also allowing EON to make a dividend payout (Hong Leong Bank – EON Bank Merger Process & 100-Day Achievement Report, August 2011).

As for Bumiputra-Commerce Holdings Berhad (BCHB) and Southern Bank Berhad (SBB), BCHB who was Malaysia's second largest lender made a proposal to acquire SBB in October 2005, which was also being seen as the start of another round of merger in Malaysia banking industry. BCHB was looking to strengthen its domestic position prior to its regional expansion. SBB is a bank which focuses on wealthy individuals, housing and car loans, and also loans to SME businesses, which BCHB believed provided a great synergy and complement the then BCHB portfolio on the consumer banking on top on its investment banking service.

> *"What Commerce stands to gain from such a merger are the following:*
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> *a. A very financially sound medium-sized banking group – RWCR of 14.8% for the group (16.4% for the bank) and a net NPL ratio of just 9%*
> *b. Southern Bank's strong retail franchise in commercial banking*

c. Southern Finance, given that CAHB's finance division is weak
d. *BHL Venture, which greatly enhances the size of Commerce's CIMBPrincipal"*

(Affin Research, 24 October 2005)

After five months, BCHB successfully acquired SBB in first half of 2006, and then it underwent a major restructuring exercise to transform itself into a universal bank. The restructuring started with Bumiputra-Commerce Holdings Berhad (BCHB), which is the listed vehicle of CIMB Group transferring all its operating entities to CIMB Group. This makes CIMB Group the listed company and also the parent company of all its operating entities. There are four major legal entities created under CIMB Group during the restructuring exercise which are CIMB Bank Berhad, CIMB Islamic Bank Berhad, CIMB Investment Bank Berhad, and PT Bank Niaga.

CIMB Bank is the commercial banking arm consists of the former Bumiputra-Commerce Bank and Southern Bank. CIMB Islamic Bank is the combination of previous CIMB Islamic financial boutique and Commerce Tijari Bank. Last but not least, CIMB Investment Bank consists of the Commerce International Merchant Bankers and GK Goh Securities from Singapore. PT Bank Niaga remains status quo as CIMB's commercial banking arm in Indonesia.

1.1.1 INTRODUCTION OF CIMB AND SOUTHERN BANK

CIMB Group or CIMB in general, is one the leading universal bank in ASEAN region. CIMB is one the top five banks in ASEAN and has the largest branch network in this region. Besides, CIMB has the largest investment bank franchise in Asia Pacific (excluding Japan). This is largely a result of the regional and overseas acquisitions done by CIMB after the M&A with SBB managed to strengthen its foothold in Malaysia. CIMB has purchased Bank Niaga and Bank Lippo from Indonesia, Bank Thai from Thailand, Bank of Commerce from Philippines and Royal Bank of Scotland's Asia Pacific investment banking business from year 2008 to 2012. The timeline chronology of CIMB history is attached in appendix 3.

CIMB Group is inclusive of CIMB Investment Bank, CIMB Bank, CIMB Islamic, CIMB Niaga, CIMB Securities International and CIMB Thai across ASEAN. The group operates in a parallel dual banking model of CIMB Conventional banking business and CIMB Islamic banking business which is Syariah compliant. Their banking business covers Retail Banking, SME Banking, Corporate & Institutional Banking, Treasury and Wholesale, Group Asset Management and Insurance with Takaful.

CIMB is a result of multiple M&As during the past few decades, with its head quarter currently sitting in Kuala Lumpur. Southern Bank was one of the bank merge into CIMB we see today. CIMB currently has around 40,000 employees reaching out to more than 80% of ASEAN population representing 89% of the region's gross domestic product(CIMB Group Annual Report, 2010).

CIMB mainly operates in ASEAN, with its strong presence also in Asia Pacific, CIMB has the capability assist their customers and investors to go beyond ASEAN reaching out to any opportunities in Asia Pacific.

Southern Bank Berhad prior to merger with CIMB provides banking and related financial services in Malaysia. It offers commercial banking, hire purchase, securities trading, fund management, unit trusts, venture capital, investment banking, nominee services, as well as insurance products. The company also provides various services in loans application and advisory services, and trade services, and business solutions to its corporate and commercial clients.

In addition, Southern bank provides online banking system services, which enables businesses to perform online transactions and manage their finances from their office locations.

Southern bank’s corporate financial services include corporate lending, trade finance, project finance, loan syndication, financial and project advisory, and electronic banking solutions, as well as wealth management services.

Last but not least, Southern bank’s consumer banking services include current and savings accounts, personal loans, home mortgages, credit cards, and fixed deposits. It has strategic alliances with Master Card International, American International Group, The Conference Board of New York city, Japan Credit Bureau, Securities Clearing Automated Network, and Women’s institute of management.

1.2 PURPOSE OF STUDY

This study aimed at analysing how synergies has been realised from M&A and post M&A from multiple angle point of view. Meanwhile most other M&A synergy study applies only quantitative measurement to measure synergies, which measures only 1 or 2 very specific parameter or arguments involved in M&A in order to prove synergy value creation or destruction, this case study uses both quantitative and qualitative approach that allows collection of inputs from various sources from different point of view. It enables a synergy of M&A to be analysed and researched from various observation dimensions, hence gathering a richer feedback and generating an observation that triangulates each other in the big picture. Inputs being collected to complete this case study including annual reports and financial figures, interviews, participant observations, articles, news, and market research reports.

Many company started M&A effort with the intention to achieve inorganic growth and synergies in value creation. All of them believe and expect that they would achieve a "1+1>2" synergies by doing M&A, but many of them are not very sure that it will happened, nor did they know whether has it been achieved post M&A.

In this study, I will evaluate synergy creation by conducting interviews with parties involved in the M&A, using secondary data as supplement.

I will be identifying the background, motive and synergies expected by the acquirer pre-M&A, and hence, evaluating processes and values gained post M&A versus the initial motives of M&A. This is because synergies does not just exist and get created by itself, it will only exist through being actively managed to create synergies expected according initial motives of the M&A.

1.3 IMPORTANCE OF STUDY

This study contributes to understanding of BCHB-SBB M&A synergy creation. Meanwhile many M&A have led the acquirer to nowhere or even value destruction (Sufian et al., 2007), the BCHB-SBB M&A is a very interesting example to look at. During the period where BCHB have just acquired SBB, it was generally branded as a hostile takeover by the market.

> *“Southern Bank is resisting a merger bid from bigger rival CIMB, a unit of Malaysia's second top banking group Bumiputra-Commerce Holdings. CIMB is pursuing merger talks with two key shareholders in Southern Bank, despite opposition from Southern's board of directors who wants the country's No 9 lender to remain independent. In a move to make it more difficult to mount a hostile takeover, Southern Bank has been buying its own shares from the market.”*
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> *(Business Times, 9 November 2005)*

> *“The Malaysian press viewed the offer as predatory. Researchers say that some of the depositors of SBB have more confidence in SBB than in BCHB due to BCHB's records of being unable to survive recession.”*
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> *(Institutional Shareholder Services, 2006)*

Market was generally in doubt whether this M&A that looks too good to be true to harvest synergies that it intended to achieve. Although the two entities looks perfectly fit for each other to complement each other's strengths and weaknesses, market believed that this hostile takeover have demoralised staffs from SBB hence driving them to leave the merged entity. Notwithstanding the fact that M&A integration processes is a tough challenge for any M&A, negative perceptions given to SBB staffs on this hostile takeover and resistance from staffs does not help in this context. Losing talents and expertise, which is the most valuable asset of acquiring SBB could seriously harm BCHB's intention to grow its retail banking arm with no synergy achieved from this M&A.

> *"Not an easy integration : On paper SBB is a nice fit for BCH. It brings much-needed capability and positioning in the critical SME and consumer banking space… Upside? Yes. Alchemy? Unlikely. Dato Nazir and team confront many lofty issues and are living on a large promise. The expectation and execution burden is massive and growing... Investment bankers have a weak track record at managing retail/commercial banks – resolving cultural conflicts and dealing with employee issues. A bonus doesn't always bring the ranks into line."*
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> *(Morgan Stanley Equity Research, 16 March 2006)*

> *"There is no guarantee that the merged entity will do well. According to analysts, BCHB will take a few years before it can financially bounce back from the said acquisition. Therefore, this may result in negatively affecting shareholder value in the long-term."*
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> *(Institutional Shareholder Services, 2006)*

Despite doubts from market researchers and analyst on this M&A achieving synergies, CIMB Group which is the result of this M&A with post-merger restructuring, has been doing very well in Malaysia as well as ASEAN to date, being the top 5 banking groups in ASEAN, having footprints in almost every ASEAN country. CIMB is today covering around 10-15% of lending portfolio in Malaysian banking market(CIMB Analyst Presentation 4Q11, 27 February 2012) funding many major economic activities in Malaysia. It is also one of the few Government Linked Companies(GLC) that has really performed well the past few years compared to other GLCs.

Therefore, I will be drilling into details to look at what are the synergies that BCHB-SBB M&A has realised from the angle of financial strength, operation efficiency, market captured, knowledge sharing and etc. And I will also be able to understand how this synergised new CIMB entity post M&A able to maximise the advantage gained from this M&A and progress faster than other domestic banks.

By conducting this case study, we are gaining more insights into synergies of M&A other than just growth in accounting figures such as profits and earnings. We are able to understand more on other qualitative factors and synergies gained that could possibly be the hidden X factors that is providing the extra strength to the then acquirer to develop into a stronger and better player in the banking industry today.

1.4 ORGANIZATION OF STUDY

This case study consists of 5 chapters. Chapter 1 will be a brief introduction to M&As, M&As in Malaysia banking sector and also introduction to CIMB and SBB.

Chapter 2 presents the literature review that I did for this study. In this chapter, I will gain some insight on the theories on M&A, the motive behind M&A, and synergies achieved by executing M&A.

Chapter 3 underlines the research methodology applied in this study.

Chapter 4 will be discussing about the analysis and results of this study using with qualitative method according to interview feedbacks supported by quantitative financial ratios.

Chapter 5 is presenting the summaries and conclusions on this study.