COMPARATIVE STUDY OF FINANCIAL PERFORMANCE BEFORE AND AFTER MERGER OF COMMERCIAL BANKS IN NEPAL

A Dissertation Proposal

Submitted by

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Declaration

I hereby declare that this dissertation proposal, entitled **"**Comparative Study on Financial Performance Before and After Merger of Commercial Banks in Nepal**"** is my original work and has been prepared in accordance with the academic and ethical standards of the institution. I confirm that this proposal is free from plagiarism, fabrication, falsification, duplication, or any other form of academic misconduct. All sources of information and ideas used have been properly acknowledged and cited.

So, I acknowledge that, should any breach of academic integrity or originality be identified at any stage, I shall bear full responsibility and accept any decision or disciplinary action taken by the concerned authority in accordance with the dissertation guideline.

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Student's Name: Bhuwan Bhattarai

Submission Date: 2083-01-17(30th April, 2026)

Approval Sheet

The dissertation proposal titled "Comparative Study on Financial Performance Before and After Merger of Commercial Banks in Nepal" submitted by Bhuwan Bhattarai as a partial fulfillment of Masters of Business Studies(MBS) is technically accepted and he/she has successfully defended the proposal with confidence about claim, plan and justification. So, It is approved to forward the dissertation report writing process and complete timely. We hope that he/she will accomplish it successfully in accordance to the proposal under the norms, rules and format of the dissertation guideline issued by office of the Dean or Faculty of Management.

Best of Luck !

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Faculty Member	Chairman, MRSC	Cordinator,MBS Program

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Assignment of Supervisor:

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CHAPTER I

INTRODUCTION

1.1 Background of the Study

The history of Nepalese banking industry began in 1937 AD with the establishment of the Nepal Bank Limited as the country's first commercial bank with shared ownership by the government and the general public. The Nepalese financial industry has seen significant changes in the financial sector rules and regulations during the past 50 years since the establishment of Nepal Bank Limited. Many foreign banks have formed joint venture banks in Nepal as a result of economic liberalization and a shift in emphasis toward the development of the private sector, and the Nepalese financial system has seen a great growth of the banking industry as a result of the 1980s' liberalized economic policies. After restoration of democracy, the government of Nepal has taken liberal policy in banking sector. Liberalization in banking sector started after 2040 B.S. Mergers and acquisitions (M&A) have become a globally acknowledged phenomenon. To gain the competitive advantage and increase the profit, the organizations takes the path to enter into business with other companies either by selling off the unprofitable divisions or by acquiring assets like technology, skilled workforce, etc. The recent past witnessed a rise in the number and capital investment in M&A deals across all over the world including Nepal.

Merger & acquisition have been considered synonymous because both terms serve a similar purpose, i.e., achieving sustainable performance. Hogan and Overmyer-Day (1994) provide evidence that merger associates business assets, giving equal control via an agreement, and acquisition includes purchasing of business assets of one organization by the other as a complete buyout. The difference between merger and acquisition can be explained by the mode adopted by the firms while collaborating (Roberts et al., 2003). Therefore, due to the evidence of the previous research, M & A are taken as a substitute for one another in the current study.

Merger and acquisition is a very important tool for the expansion of business in different countries and the researchers from all over the world are taking interest to work in this field (Goyal and Joshi 2011). If we go into the history of Merger and Acquisition, M & A were started from the United States back in the eighteen century. In

Europe, the M & A begins in nineteen century (Focarelli, Panetta and Salleo 2002). Maximum research on M & A has been done in the United States and Europe market. Comparatively little research work had been done on M & A in the developing countries like Pakistan, India, Malaysia and Bangladesh etc.

According to Singh (1971), a takeover is a business practice wherein one firm takes over the other and controls more than 50% of the equity of the acquired firm. A merger is when at least two firms are combined as a new legal entity. As per this definition, it can be a+b=c. Viewed from this angle, where there is a balance of power between the merging enterprises, it can be a new entity with a different name after the merger.

The Nepalese financial sector has been experiencing significant changes since the 1980s when the government adopted the financial sector liberalization process (Gajurel & Pradhan, 2012). Flexible licensing policy and deregulation in the financial sector encouraged foreign joint venture banks, domestic private banks, and finance companies to operate in the Nepalese Market (Gajurel & Pradhan, 2012). The trend of establishing banks and financial institutions (BFIs) grew more and more. By December 2011, the number of commercial banks, development banks, and finance companies reached 31, 87, and 79, respectively.

Mergers and acquisitions are vital tools to facilitate the financial industry's sound and efficient performance while subjugating the system's underlying problems. The instrument also plays a crucial role in bringing down the cost of operations and increasing the market competitiveness and profitability of the firms (Gautam, 2016).

1.2 Problem Statement

The banking sector in Nepal has experienced a significant wave of mergers and acquisitions following the policies introduced by Nepal Rastra Bank to strengthen financial stability, improve operational efficiency, and enhance the competitiveness of commercial banks. Although mergers are expected to improve financial performance through economies of scale, better resource utilization, and increased market share, previous studies have reported mixed findings regarding their actual impact. Some researchers have found improvements in profitability, liquidity, and capital adequacy after mergers, while others have reported declines in return on assets, return on equity, and loan quality. These inconsistent findings indicate that the effectiveness of mergers in improving the financial performance of Nepalese commercial banks remains uncertain.

Moreover, most previous studies have examined only a limited number of financial indicators or focused on a small sample of banks, creating a research gap in understanding the comprehensive impact of mergers on financial performance. Therefore, it is necessary to conduct a comparative analysis of the financial performance of commercial banks before and after merger using key financial indicators such as Capital Adequacy Ratio (CAR), Non-Performing Loan (NPL), Spread Ratio (SR), Net Profit Margin (NPM), Return on Assets (ROA), Return on Equity (ROE), Earnings per Share (EPS), and Cash to Total Assets (CTA). This study seeks to determine whether there are significant differences in these financial performance indicators before and after the merger of commercial banks in Nepal.

- What is the profitability of commercial banks before and after merger using Net Profit Margin (NPM), Return on Assets (ROA), Return on Equity (ROE), and Earnings per Share (EPS).
- Does the liquidity and capital adequacy position of commercial banks before and after merger using Cash to Total Assets (CTA) and Capital Adequacy Ratio (CAR).
- What are the changes in asset quality and operational performance before and after merger using Non-Performing Loan (NPL) and Spread Ratio (SR).

1.3 Objective of the Study

i. To compare the profitability of commercial banks before and after merger using Net Profit Margin (NPM), Return on Assets (ROA), Return on Equity (ROE), and Earnings per Share (EPS).
ii. To examine the liquidity and capital adequacy position of commercial banks before and after merger using Cash to Total Assets (CTA) and Capital Adequacy Ratio (CAR).
iii. To analyze the changes in asset quality and operational performance before and after merger using Non-Performing Loan (NPL) and Spread Ratio (SR).

1.4 Rationale of the Study

Mergers and acquisitions have become an important strategy in the Nepalese banking sector for improving financial stability, operational efficiency, competitiveness, and profitability. However, previous studies have reported mixed results regarding the actual impact of mergers on the financial performance of commercial banks. Therefore, this study is undertaken to compare the financial performance of selected commercial banks before and after merger and to determine whether significant changes have occurred in their financial position. The study focuses on important financial indicators such as Net Profit Margin, Return on Assets, Return on Equity, Earnings per Share, Capital Adequacy Ratio, Non-Performing Loan, Spread Ratio, and Cash to Total Assets. The findings are expected to provide useful information to bank management, investors, shareholders, policymakers, and other stakeholders in understanding the financial consequences of mergers and acquisitions. Furthermore, the study contributes to the existing literature by providing comparative evidence on the financial performance of selected merged commercial banks in Nepal.

1.5 Limitations of Study

- The study covers only selected commercial banks in Nepal that have undergone mergers and acquisitions.
- Only eight merged commercial banks are selected as the sample, which may limit the generalizability of the findings.
- The study is based mainly on secondary data obtained from annual reports and related publications.
- The study considers only selected financial indicators: CAR, NPL, SR, NPM, ROA, ROE, EPS, and CTA.
- Non-financial factors such as employee satisfaction, customer satisfaction, management practices, organizational culture, and technological integration are not examined in detail.
- The financial performance may be affected by economic, regulatory, market, and bank-specific factors that are not separately controlled.
- The study uses limited statistical tools such as mean, standard deviation, correlation, and t-test for analysis.
- The availability and reliability of published secondary data may affect the accuracy and consistency of the findings.
- The study is subject to limitations of time, resources, study period, sample size, and methodology.

1.6 Organization of the Report

The fundamental purpose of the proposed study is to fulfill the partial requirements for the MBS Degree from Tribhuvan University. Therefore, the organization to the study report will be made accordingly. The first chapter will be the introduction of the study. It will contain background information, statement of the problem, objectives, significance, limitations, and organization of the study. The second chapter will be assigned for review of the literature. It will organize with the conceptual review, review of related studies, and concluding remarks to express the research gap. After the review of the literature, the subsequent chapter will be a methodological aspect. Therefore, the third chapter will be presented as a research methodology. It will contain research design, sampling process, data collection procedure, analysis techniques, model, explanation of variables, and methodological limitation will also express. The fourth chapter will be assigned to data presentation and analysis. As an important part of the research, this chapter will organize with different sections as per the study aspects. Specifically, it will contain variable based data, descriptive statistics, inferential statistics and their analysis. At the end of this chapter, findings and discussion will be made. The fifth and final chapter will be assigned for summary, conclusion, and recommendations. Bibliography and relevant annexes will be presented at the end.

CHAPTER II
LITERATURE REVIEW

2.1 Theoritical Review

Different theories are investigated to explain the main motives of M&A in the banking sector. Such theories include synergy, market and corporate control, and free cash flow. These theories enhance financial performance after M&A (Mantravadi and Reddy, 2008). According to Neary (2007), there are two significant reasons for M&A in business organisations: efficiency gain and strategic rationale. The efficiency gain is achieved when two firms integrate and use their resources jointly. The strategic rationale is achieved through the M&A process, which leads to changes in the structure of the combined entity that positively impact the company's profitability. Seth (1990) suggests that M&As occur in the financial industry due to value-maximising and managerial theories. However, the author posits that no clear evidence exists. Most of the past research in the banking industry produces mixed evidence that M&A creates value for shareholders. Ayadi et al. (2013) suggest that M&A results create shareholder value through market power or efficiency gain. This view contradicts the findings of Kalra et al. (2013) and Liargovas and Repousis (2011), whose results suggest that M&A does not create shareholders' wealth. DeYoung et al. (2009) summarise 150 recent studies on M&A in financial institutions. The findings show that literature prior to the year 2000 suggests that efficiency improved in financial institutions in Europe, the USA, and North America more broadly. However, event study literature showed mixed results about the wealth effect on shareholders. Similarly, post-2000 literature suggests the impact of M&A on bank performance in the U.S. and Europe has produced mixed results on geographic and product diversification and resulted in adverse impacts on depositors, borrowers, and other external stakeholders (DeYoung et al., 2009).

2.2 Empirical Review

Shrestha et al. (2017) investigated the impact of mergers on Nepalese banking and financial institutions using six BFIs and 120 respondents. The study revealed deteriorating loan quality and declines in ROA and ROE post-merger, concluding that mergers alone could not resolve institutional challenges without addressing other underlying factors. Joshua (2011) examined the comparative analysis of the impact of merger and acquisitions on financial efficiency of bank in Nigeria. Using convenience judgment sample selection method, data were collected from annual report of the selected sample banks. This study employed t –test statistics and found that post –merger and acquisition period was more significantly improved then the pre-merger period.

Dhakal (2019) analyzed the impact and challenges of mergers and acquisitions in Nepalese banks using descriptive research and surveys of employees and customers. While post-merger phases showed improvements in shareholder value, positive customer outcomes, and employee satisfaction, challenges such as HR conflicts, BOD formation, IT integration, and procedural issues were identified, emphasizing the importance of socio-cultural and operational considerations during M&A. Patel (2017) analyzed the pre and post-merger financial performance: An Indian perspective. This paper compares the before and after merger position of selected Indian banks. This study found a negative impact of merger on ROE, ROA, NPM, Yield on advance and yield on investment and, EPS ,profit per employee and business per employee have shown positive trend after the merger.

Bajgai and Pradhan (2021) examined an assessment of financial performance and service facility improvement after merger and acquisition of financial institutions of Nepal .using cross-sectional study conducted among the 385 employees of banking sector. This study identified that the financial performance and service quality of both types of banks (category A and B) was significantly difference in post-merger situations. The study found that indicators like EPS, MPS and debt ratio have improved. Adhikari (2023) examined the pre and post-merger financial performance analysis of commercial banks in Nepal. This paper employs a descriptive and casual comparative research design to examine financial performance, involved in six merger banks. Mean standard deviation, paired sample t-test, Pearson correlation, regression analysis using for data analysis. This paper found that positive correlations between pre and post-merger period for EPS, NWPS, CDR, CAR, NPL, ROA, ROE and NPM excluding P/E ratio.

Adhikari et al. (2023) analysed the effect of merger and acquisitions on the financial performance of commercial banks in Nepal using a Descriptive and casual-comparative. This study used NRB financial stability report and bank audit report of seven commercial banks, engaging 13 financial ratios above three years period before and after merger. Paired t test has used for analysis. The finding financial performance of commercial banks improved significantly after the merger, as measured by liquidity and leverage ratio but ratio of probability and shareholders wealth show no change. Similarly, bank merger have produced mixed result.

Kandel (2024) investigated the impact of mergers and acquisitions on the profitability and stability of Nepalese bank; a comparative analysis using quantitative research design. Multiple regressions were applied to determine the relationship between pre and post-merger period. This study found positive and correlation between EPS, ROA and P/E ratio with ROE Fatima and shehzad (2014) examine the analysis of impact of merger and acquisition of financial performance of banks; A case of Pakistan. This study used six financial ratios for analysis and ten banks are selected for analysis. This study founding only ROE is affected by the merger and acquisitions and other ratio have no impact after the merger.

2.3 Research Gap

Previous studies on mergers and acquisitions in Nepalese commercial banks have produced mixed and inconsistent findings. Some studies have reported improvements in financial performance after mergers, while others have found declines or insignificant changes in indicators such as ROA, ROE, profitability, and loan quality. Moreover, many previous studies have focused on a limited number of banks, financial indicators, or specific aspects of merger performance. The existing literature therefore does not provide sufficient comprehensive evidence regarding the overall financial performance of commercial banks before and after merger. This study attempts to address this gap by comparatively analyzing selected merged commercial banks using a broader set of financial indicators, including CAR, NPL, SR, NPM, ROA, ROE, EPS, and CTA. Thus, the study aims to provide additional empirical evidence on whether mergers have resulted in significant changes in the financial performance of selected commercial banks in Nepal.

CHAPTER III
RESEARCH METHODOLOGY

This study adopts a descriptive and inferential research design to compare the financial performance of commercial banks in Nepal before and after merger. The descriptive research design is used to present and summarize the financial performance of the selected banks, while the inferential research design is applied to examine whether significant differences exist between the pre-merger and post-merger periods.

The study is based on a quantitative research approach using secondary data. The population comprises all commercial banks in Nepal that have undergone merger and acquisition. Out of the merged commercial banks, eight banks are selected as the sample through simple random sampling. The sample banks include NIC Asia Bank Ltd., Global IME Bank Ltd., Prabhu Bank Ltd., Bank of Kathmandu Ltd., NMB Bank Ltd., Laxmi Bank Ltd., Sanima Bank Ltd., and Mega Bank Ltd.

3.1 Research Design

This study uses a Descriptive and inferential research design. Descriptive research design is important to describe the characteristics of a population or a particular phenomenon and analytical research design aims to understand phenomena by discovering and measuring causal relations among them. In this research, through descriptive and inferential study, how merger and acquisition impact pre-post financial performance of commercial bank is being studied.

3.2 Nature and Source of Data

The study is based on quantitative and secondary data. The required financial data are collected from the annual reports of the selected commercial banks, particularly from their profit and loss accounts, balance sheets, and other relevant financial statements and publications. In addition, related information is obtained from Nepal Rastra Bank (NRB), Nepal Stock Exchange (NEPSE), and other relevant sources. The collected data are used to compare the financial performance of selected commercial banks before and after merger using the selected financial indicators.

3.3 Papulation and Samling

The population of this study consists of all commercial banks in Nepal that have undergone merger and acquisition. According to the proposal, there were 26 commercial banks operating in Nepal, and those that experienced merger and acquisition constitute the target population for this research. Since the study aims to compare financial performance before and after merger, only merged commercial banks are considered.

S. No.	Name
1	Kumari Bank (After the merger with Nepal Credit and Commerce Bank)
2	Rastriya Banijya Bank
3	Agriculture Development Bank
4	Nabil Bank (After the acquisition of Nepal Bangladesh Bank)
5	Nepal Investment Mega Bank (After the merger with Mega Bank Nepal Limited)
6	Standard Chartered Bank Nepal
7	Himalayan Bank (After the merger with Civil Bank Limited)
8	Nepal SBI Bank
9	Everest Bank
10	Prabhu Bank (After the acquisition of Century Bank Limited)
11	Laxmi Sunrise Bank (After the merger with Sunrise Bank)
12	Global IME Bank Limited (After the merger with Bank of Kathmandu)
13	Citizens Bank International Limited
14	Prime Commercial Bank
15	NMB Bank Nepal
16	NIC Asia Bank
17	Siddhartha Bank
18	Sanima Bank
19	Machhapuchchhre Bank
20	Nepal Bank Limited

3.4 Sampling Methods

A sample is a subset of the population selected for detailed investigation. In this study, eight merged commercial banks are selected using the simple random sampling technique. The sample banks are NIC Asia Bank Ltd., Global IME Bank Ltd., Prabhu Bank Ltd., Bank of Kathmandu Ltd., NMB Bank Ltd., Laxmi Bank Ltd., Sanima Bank

Ltd., and Mega Bank Ltd. These banks are selected to represent the population and to facilitate a comparative analysis of their financial performance during the pre-merger and post-merger periods.

3.5 Data collection Tools

Quantitative nature of secondary data has been used for conducting the study. The secondary sources of data has been collected from the website of respective commercial banks annual reports especially from profit and loss accounts, balance sheet and other publications made by banks. Likewise some other related information are gathered from related banks and related agencies like Nepal Rastra Bank, sharesansar, Nepal Stock Exchange Limited.

3.6 Research Framework and Definition of Variables

3.6.1 Models

The study examines the effect of merger and acquisition (independent variable) on the financial performance (dependent variables) of commercial banks in Nepal. Financial performance is measured using eight financial indicators: Capital Adequacy Ratio (CAR), Non-Performing Loan (NPL), Spread Ratio (SR), Net Profit Margin (NPM), Return on Assets (ROA), Return on Equity (ROE), Earnings per Share (EPS), and Cash to Total Assets (CTA).

Therefore, the basic relationship functions are expressed as follows:

Pre-Merger Regression Model

The financial performance of Bank A and Bank B can be measured using ROA, ROE, and EPS as dependent variables, while capital adequacy ratio, non-performing loan, spread ratio, net profit margin, cash-to-total-assets ratio, and other indicators are independent variables.

$ROA = \beta_0 + \beta_1 CAR + \beta_2 NPL\ \beta_3 SR + \beta_4 NPM + \beta_5 ROE + \beta_6 EPS + \beta_7 CTA + \varepsilon$

$ROE = \beta_0 + \beta_1 CAR + \beta_2 NPL\ \beta_3 SR + \beta_4 NPM + \beta_5 ROA + \beta_6 EPS + \beta_7 CTA + \varepsilon$

$EPS = \beta_0 + \beta_1 CAR + \beta_2 NPL\ \beta_3 SR + \beta_4 NPM + \beta_5 ROE + \beta_6 ROA + \beta_7 CTA + \varepsilon$

Where:

- CAR = Capital Adequacy Ratio
- NPL = Non-Performing Loan
- SR = Spread Ratio

- NPM = Net Profit Margin
- ROA = Return on Assets
- ROE = Return on Equity
- EPS = Earnings Per Share
- CTA = Cash to Total Assets Ratio
- β_0 = Constant
- β_1–β_7 = Regression coefficients
- ε = Error term

3.6.2. Post-Merger Regression Model

After the merger, the same determinants can be examined to determine their influence on the combined financial performance of Bank A & B.

$$ROA = \beta_0 + \beta_1\, CAR + \beta_2\, NPL\ \beta_3\, SR + \beta_4\, NPM + \beta_5\, ROE + \beta_6\, EPS + \beta_7\, CTA + \varepsilon$$

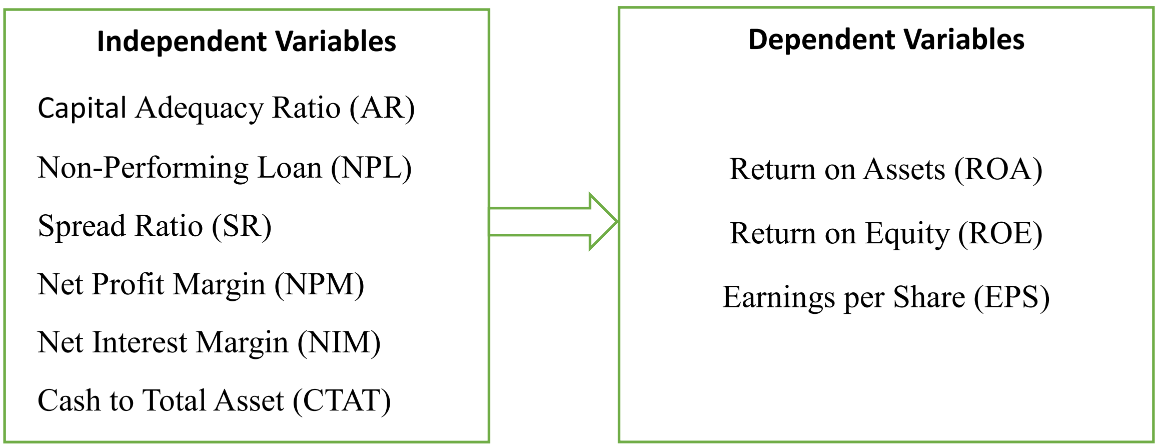
$$ROE = \beta_0 + \beta_1\, CAR + \beta_2\, NPL\ \beta_3\, SR + \beta_4\, NPM + \beta_5\, ROA + \beta_6\, EPS + \beta_7\, CTA + \varepsilon$$

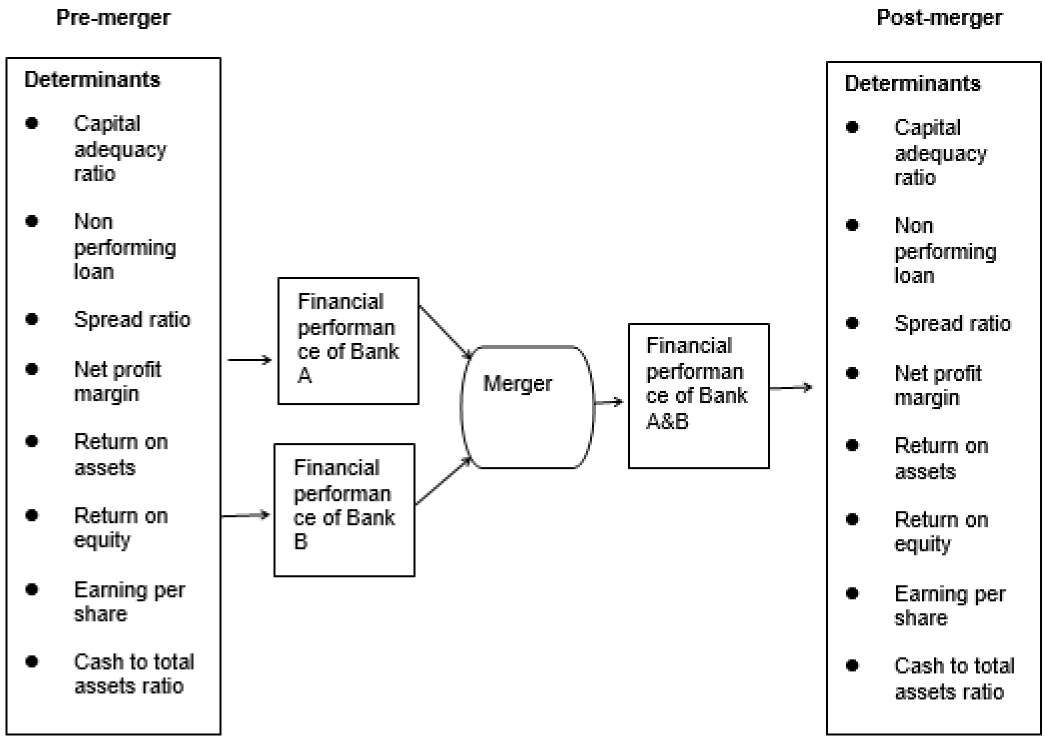
$$EPS = \beta_0 + \beta_1\, CAR + \beta_2\, NPL\ \beta_3\, SR + \beta_4\, NPM + \beta_5\, ROE + \beta_6\, ROA + \beta_7\, CTA + \varepsilon$$

Where:

- CAR = Capital Adequacy Ratio
- NPL = Non-Performing Loan
- SR = Spread Ratio
- NPM = Net Profit Margin
- ROA = Return on Assets
- ROE = Return on Equity
- EPS = Earnings Per Share
- CTA = Cash to Total Assets Ratio
- β_0 = Constant
- β_1–β_7 = Regression coefficients
- ε = Error term

3.6.3 Research Framework and Variables





Hypothesis

H1: Capital adequacy ratio has a significant effect on the financial performance of banks.

H2: Non-performing loan has a significant effect on the financial performance of banks.

H3: Spread ratio has a significant effect on the financial performance of banks.

H4: Net profit margin has a significant effect on the financial performance of banks.

H5: Return on assets has a significant effect on the financial performance of banks.

H6: Return on equity has a significant effect on the financial performance of banks.

H7: Earnings per share has a significant effect on the financial performance of banks.

3.7 Methods of Analysis

Both descriptive and inferential statistics tools are used for analysis of data. Mean, standard deviation, correlation and T-test are used for the purpose of presentation and analysis of data. Microsoft Excel and E Views are used for the presentation, classification, and analysis of the data.

Return on Assets (ROA): Return on Assets measures the efficiency with which a bank utilizes its total assets to generate net profit. A higher ROA indicates more effective utilization of assets (Brigham & Houston, 2022).

$$\text{ROA} = \frac{\text{Net profit after tax}}{\text{Total assets}}$$

Return on Equity (ROE): Return on Equity measures the return earned on shareholders' investment. It evaluates the effectiveness of management in generating profits from shareholders' equity (Ross, Westerfield, & Jaffe, 2019).

$$\text{ROE} = \frac{\text{Net profit after tax}}{\text{Share holder fund}}$$

Earnings per Share (EPS): Earnings per Share represents the amount of net profit attributable to each outstanding ordinary share. EPS is widely used by investors to assess profitability and investment performance (International Accounting Standards Board, 2023).

$$\text{EPS} = \frac{\text{Net Income - Prefered Dividends}}{\text{End of Period Common Shares Outstanding}}$$

Capital Adequacy Ratio (CAR): Capital Adequacy Ratio measures a bank's ability to absorb financial losses and protect depositors by maintaining adequate capital against risk-weighted assets. A higher CAR indicates greater financial strength and stability (Bank for International Settlements, 2019).

$$\text{CAR} = \frac{\text{Tier 1 Caital + Tier 2 Capital}}{\text{Risk-Weighted Assets}}$$

Non-Performing Loan (NPL): Non-Performing Loan is the proportion of loans on which borrowers have failed to make scheduled principal or interest payments for a specified period. A lower NPL ratio reflects better asset quality and effective credit risk management (International Monetary Fund, 2019).

$$\text{NPL to TL} = \frac{\text{Non-performing Loan}}{\text{Total Loan and Advance}}$$

Spread Ratio (SR): Spread Ratio represents the difference between the average lending rate and the average deposit rate of a bank. It reflects the bank's efficiency in generating income from its core lending activities. A higher spread generally indicates improved earning capacity (Nepal Rastra Bank, 2024).

$$\text{SR} = \frac{R_p - P_f}{\sigma_p}$$

Net Profit Margin (NPM): Net Profit Margin measures the percentage of net income earned from total operating income. It indicates how efficiently a bank converts its revenue into net profit after deducting all expenses (Brigham & Houston, 2022).

$$\text{NIM} = \frac{\text{Net Interest Income}}{\text{Average Interest-Earning Assets}}$$

Cash to Total Assets (CTA): Cash to Total Assets measures the proportion of total assets held in cash and cash equivalents. It reflects the liquidity position of a bank and its ability to meet short-term obligations (Rose & Hudgins, 2013).

$$\text{Cash to Total Assets (CTA)} = \frac{\text{Total Cash}}{\text{Total Assets}})$$

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Appendix – i

An article on A Comparative Analysis of the Financial Performance of Commercial Banks after Merger and Acquisitions Using Nepalese Data by Marie Kavanagh & Bonnie Hampson

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A comparative analysis of the financial performance of commercial banks after mergers and acquisitions using Nepalese data

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A B S T R A C T

This article investigates consolidation and restructuring in the banking sector in Nepal that was induced by regulatory intervention in recent years. We compare the financial performance of the overall commercial banking sector and selected commercial banks on an individual basis before and after the mergers and acquisitions (M&A) policy intervention. The research employs an analysis of the financial ratios (profitability, liquidity, leverage, and wealth of shareholders ratios) before and after mergers that took place between 2013 and 2020 on a sample of seven Nepalese commercial banks. Hypotheses are tested using a paired sample *t*-test to measure any significant difference between the pre- and post-merger situations of the acquiring banks' financial metrics. The findings indicate that the overall commercial banking sector significantly improved their liquidity and leverage ratios in the post-merger period. Other measures, such as the profitability and shareholder wealth ratios showed either mixed or insignificant results after the M&A. The results for selected commercial banks on an individual basis were even less conclusive and mixed. While some banks showed improvement in financial ratios, other results were insignificant.

1. Introduction

The consolidation of banks and financial institutions (BFIs) through mergers and acquisitions (M&A) has been a new trend in Nepal since early 2010s. After the political reform in 1990, the phenomenal growth of BFIs in a short period resulted in financial instability in the BFIs. The central bank of Nepal (Nepal Rastra Bank) described the BFIs' functions, tasks, and responsibilities poorly, causing confusion within the sector. All BFIs in Nepal fulfil similar functions, mainly collecting deposits and distributing out loans due to limited market opportunities and the economy's small size. Furthermore, an increasing number of unregulated savings and co-operatives institutions in the cities and regional areas create unhealthy financial competition directly or indirectly, which causes a financial vulnerability for the BFIs' stability. The lack of balance between the deposit and loan growth rates gradually started to cause liquidity shortages and interest rate fluctuations in the banking sector, putting pressure on commercial banks' credit-to-deposit (CD) ratios. There had been a tremendous surge in non-performing loans and corporate governance failures in the banking sector before the M&A policy. As a result, the central bank Nepal Rastra Bank (NRB) enacted the 'Mergers Bylaws 2011' to ensure financial stability in BFIs and strengthen the financial sector's operational efficiency by cutting costs, diversifying risks, and strengthening their capital base. Table 1 provides an overview of the growth of different BFIs and their types.

In the monetary policy report 2015/2016 published in July 2015, the NRB directed BFIs to fulfill the minimum new capital requirement by mid-July 2017. After these directives, commercial banks required Nepalese rupees (Rs) 8 billion, up from Rs 2 billion; development banks needed Rs 2.5 billion, up from Rs 0.64 billion; and finance companies required Rs 0.8 billion, up from Rs 0.3 billion. BFIs that failed to meet the new capital requirement would face restrictions on opening new branches and declaring dividends or bonus shares. Following that guidance, the number of development banks and finance companies was successfully reduced through M&A deals among BFIs in accordance with the new capital requirements (see Table 1). However, these deals did not result in a substantial reduction in the number of commercial banks immediately. Nevertheless, according to the NRB Financial Stability

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Appendix – ii

An article on Pre and Post Merger Financial Performance Analysis of Commercial Banks in Nepal by Part Raj Adhikari

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Pre and Post–Merger Financial Performance Analysis of Commercial Banks in Nepal

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Abstract

Purpose: This study attempts to examine the effect of merger on the financial performance of Nepalese commercial banks.

Methodology: This paper employs a descriptive and causal comparative research design to examine the financial performance of commercial banks involved in six merger deals as of mid-July 2022, with a sample of four merger deals completed before mid-July 2018. Mean, standard deviation, paired sample t-test, Pearson correlation, regression analysis, and the VIF test, are utilized for data analysis. Financial performance is evaluated using nine key ratios (EPS, NWPS, P/E ratio, CD ratio, CAR, NPL ratio, ROA, ROE, and NPM). Secondary data covering six years (2010 to 2019), excluding the specific merging year, are analyzed.

Findings: The analysis of pre- and post-merger financial performance in the sample commercial banks revealed statistically significant differences in EPS, NWPS, ROA, and NPM. Positive correlations were observed between the pre- and post-merger periods for EPS, NWPS, CD ratio, CAR, NPL ratio, ROA, ROE, and NPM, excluding the P/E ratio. The merger proved beneficial for Nepalese commercial banks, leading to improved profitability in terms of EPS, ROA, and NPM in the post-merger phase. However, factors like CD ratio, CAR, and NPL ratio, regulated by the NRB, showed no significant changes post-merger. Although banks experienced increased P/E ratio and ROE, the impact was deemed insignificant. Notably, CAR had the most significant impact on both pre- and post-merger ROA.

Implication: The results derived from the study are relevant to managers for future merger decisions and can be used for the selection of a suitable partner for future merger activities.

Value: It contributes to a better understanding of the overall merger scenario in Nepalese banking sector, as well as the relationship between certain restrictions and merger.

Keywords: Merger, commercial banks, financial performance, ratio analysis.