



**ADDIS ABABA UNIVERSITY SCHOOL OF COMMERCE
MASTER OF CORPORATE FINANCE AND INVESTMENT MANAGEMENT PROGRAM**

**THESIS ON
“DRIVERS OF MERGER AND ACQUISITION DECISION IN ETHIOPIAN
PRIVATE BANKS”**

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**BY
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Abstract

Mergers and acquisitions refers to where two or more financial entities combine corporate resources to operate as a unit with an aim of improving their performance. Despite recent developments in every sector of the economy, the practice of mergers and acquisitions is a fairly new concept to the Ethiopian banking industry. This research aims to investigate the factors driving merger and acquisition (M &A) activity in Ethiopian Banks. With the Ethiopian government's push toward liberalization, including increased minimum capital requirements and the entry of foreign banks, local banks face heightened regulatory and competitive pressures which may lead banks to consider mergers and acquisitions. Hence, understanding the factors that may drive it is crucial. The study employed quantitative approach, using structured questionnaire to gather comprehensive insights into the perception of Ethiopian Commercial Banks towards M&A drivers. Primary data was collected from Management members of 16 private banks selected using stratified random sampling. With a response rate of 92%, 221 questionnaires have been returned and were valid for data analysis. The quantitative data was analyzed employing descriptive and inferential analysis (i.e. correlation analysis and multiple regression analysis) and using SPSS. The findings of the multiple regression indicated that only four of the predictor variables i.e. financial performance improvement, compliance with regulatory requirements, market expansion, and cost-saving synergies are the most influential factors motivating M&A decisions. Conversely, branding, diversification, and survival were not found to be statistically significant. These findings highlight regulatory compliance and financial synergies as pivotal for policymakers during sector liberalization. With an adjusted R² of 0.788, the model explains approximately 78.8% of the variance in M&A decisions, indicating a strong explanatory power. The study offers important insights for policymakers, regulators, and bank executives in planning for strategic consolidation to build a resilient and competitive banking sector in Ethiopia. Finally recommendations are made based on the findings of the study.

Keywords: *Mergers, Acquisitions, Drivers, Banks, Correlation analysis, Multiple Regression analysis.*

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Mergers and Acquisitions (M&A) are widely used corporate strategies aimed at restructuring, expanding or strengthening business operations. A merger happens when two companies join together to form a new and larger entity, while an acquisition occurs when one company acquires another company and becomes the owner of its assets and liabilities. Mergers and Acquisitions are very important strategic decisions (Kastanakis et al., 2019; Thanos & Papadakis, 2012a). These strategies are increasingly employed across sectors to improve efficiency, expand market presence, and respond to competitive or regulatory pressures. M&A is an enduring and major strategic mechanism for rejuvenating and realigning organizations when the environmental context is changing. In recent years, mergers and acquisitions have become increasingly popular not only among companies but also between financial institutions. Factors such as globalization, liberalization, internationalization of competition and technological developments have escalated this tendency.

Mergers and acquisitions (M&A) are widely recognized as key drivers of structural transformation across global industries, contributing to greater efficiency, competitiveness, and market reach. Although this trend is well-established in many parts of the world, in developing economies like Ethiopia it is still in early stages. Historically, Ethiopia's banking sector has seen few M&A activities despite being home to rapidly growing number of banks. Recently, however, there has been a noticeable shift in policy direction. The Ethiopian government has begun encouraging consolidation among private banks, sending a clear message that mergers and acquisitions are now being seen as strategic tools to build a stronger and more resilient financial system (Girma, 2022).

As of 2024, Ethiopia has over 30 private and state-owned banks, with most of them operating on small capital bases, limited market reach, and intense competition within a relatively underdeveloped financial landscape.

In recent years, the Ethiopian government and the National Bank of Ethiopia (NBE) have introduced several reforms aimed at strengthening the financial sector and encouraging consolidation. A cornerstone of these reforms is the Homegrown Economic Reform Program, which seeks to transition the economy toward a private sector-led model. Part of this strategy involves ensuring that banks are strong, well-capitalized, and competitive—both locally and internationally (Taye, 2020).

As indicated earlier, currently there are various developments that are signaling banks in Ethiopia towards mergers and acquisitions. The primary reasons include the revision of the minimum paid up capital requirement in 2021 from 2 billion birr to 5 billion birr with the deadline to raise the capital in five years (2026) from the date of enactment. Another major change is the approval of the new Banking Business Proclamation by the Ethiopian House of People's Representatives (HoPR) on mid December 2024 which officially opens the door for foreign banks to enter the Ethiopian market. This proclamation enables foreign investors to own up to 40 percent share in Ethiopian financial institutions and permits them to establish partially or fully owned foreign bank subsidiaries, open foreign bank branches, establish representative offices, or acquire shares of a bank. It also states that foreign nationals, other than foreign banks and foreign-owned Ethiopian organizations, may acquire shares in banks.

As Ethiopia moves towards liberalizing and deregulating the financial sector there is a potential for significant disruptions both at the industry and macroeconomic levels. Existing literature suggests that such structural shocks often serve as a major cause for waves of mergers and acquisitions, as institutions seek to adapt to the evolving competitive and regulatory environment.

According to the Strategic Plan of the regulatory body, the National Bank of Ethiopia has planned to implement Basel II/III frameworks by June 2025 which will further increase capital adequacy and regulatory requirements for Banks. These regulatory changes collectively signal a shift towards a more competitive and liberalized financial environment. However, there are growing concerns on whether domestic banks are adequately prepared in terms of capital as well as strategic readiness to compete with the foreign banks or to meet the regulatory standards. In response, the NBE has been consistently signaling and encouraging mergers among local banks as a proactive measure to strengthen the sector and ensure long term stability.

These changes create pressure on local banks, many of which are small, regionally concentrated and often tied to ethnic or religious affiliation, to consolidate or risk being surpassed by stronger, foreign competitors.

The Prime Minister has also hinted at the government's new direction regarding the number of banks in Ethiopia by publicly suggesting that the country doesn't need 32 banks that are inefficient and could function more efficiently with just 5 or 6 banks. He described the current banking environment as fragmented and operating more like "kiosks" rather than fully-fledged financial intermediaries indicating a lack of competitiveness and effectiveness. The ethnic and religious affiliations of the Banks was also indicated as a weakness in the sector pointing to broader challenges in governance and operation within the banking system. There are numerous factors to consider when deciding on a merger these include alignment of objectives,

potential synergy, valuation, financial health, corporate culture, market position, and technology and systems etc. Taking these factors into account, it is essential for banks to either proactively undertake voluntary mergers to meet the policy requirements or face statutory mergers that could be mandated by the NBE.

Hence, it would be appropriate time for Banks to contemplate and prepare for the upcoming merger and acquisition in the industry. Despite regulatory shifts, no study examines M&A drivers in Ethiopia's private banks which face unique ethnic/ownership constraints, post liberalization. So far only a few number of researches have been conducted on mergers and acquisitions in the Ethiopian Banking industry and this issue requires further research in light of recent and upcoming developments.

In view of this, this research is fairly new in case of the Ethiopian banking sector as it focuses on factors that may drive merger and acquisitions in Ethiopian Private Banks. These factors will be identified from the perception of Executive and Senior Management members based on the survey to be undertaken. Selected private commercial banks are taken into consideration for the purpose of conducting the study. The aim of this study is to identify strategic factors that drive merger and acquisition decision in Ethiopian banking sector.

1.2 Background of the Ethiopian Banking Sector

Following the liberalization of the banking sector in 1991, during which the Ethiopian economy was declared a free market, the market which was only occupied by state banks during the pre-1994 era has seen an influx of private banks.

At the end of June 2024, there are thirty-two banks (all of them domestic) operating in Ethiopia. Among these, two of them include the state owned banks Development Bank of Ethiopia and Commercial Bank of Ethiopia while the rest are private commercial banks. According to the NBE's second Financial Stability report, the 30 commercial banks operating in the sector have been classified as one large public bank, five medium-sized banks, and twenty-four small banks, with a consolidated capital figure of 100 billion birr as of June 2024 (which is close to USD 1.7 billion computed before the currency float (devaluation) of July 29, 2024). Nevertheless, the market is dominated by the public bank Commercial Bank of Ethiopia, which commands total assets and deposits of almost half (49.5 percent and 48.7 percent, respectively) of the entire banking sector and total capital of 24 percent. As compared to the top three ranked banks in Africa in 2024, as ranked by the African Business, i.e. Standard Bank Group (USD 12.5 billion), National bank of Egypt (USD 7.5 billion) and Attijariwafa Bank (USD 5.9 billion), the consolidated total capital of all Banks in Ethiopia combined is by far smaller.

In 2021, the Central Bank had issued a regulation which set the minimum paid-up capital required to start banking business at ETB 5 billion from previously ETB 500 million. So far, only 10 of the 30 banks have met the minimum threshold set. Even though there is still time which may allow the bigger banks to satisfy the requirement, it will still be a challenge for the majority of the second and third generation banks to achieve the minimum capital requirement.

Ethiopia has recently approved the revised Banking Business Proclamation, which repeal and replace the existing Banking Business Proclamation No. 592/2008. The approval of this Proclamation is significant in major respects, including the liberalization of the sector to foreign investment and bank mergers.

1.3 History of Bank Merger in Ethiopia

The history of mergers in the Ethiopian banking industry is limited and fairly recent. One of the earliest major consolidations happened in 1980, when the Ethiopian government merged Addis Bank and the Commercial Bank of Ethiopia to form the modern day Commercial Bank of Ethiopia (CBE) which is now the largest bank in Ethiopia. The history of Addis Bank itself was based on earlier consolidation, as it was established through the merger of Addis Ababa Bank, Banco di Roma, and Banco di Napoli, two Italian banks that operated during the imperial era.

Before the 1980 merger, only a few financial institutions had merged. For instance, the Ethiopian Investment and Savings merged with the Ethiopian Government Savings and Mortgage Company to form the then Housing and Savings Bank, which later came to be the Construction and Business Bank (CBB) in 1975.

A more recent and prominent example of consolidation happened during December 2015, when the Government Financial Enterprises Agency merged the two state-owned banks: CBB and CBE. According to the Agency, the move was intended to create a larger and more competitive giant bank that would operate on a regional and global scale. However, industry insiders pointed out that the merger was likely in response to the declining performance of CBB which was struggling to perform well in the Ethiopia's competitive banking industry (Hailemariam, 2024).

1.4 Problem Statement

Mergers and acquisitions have become widely adopted tools for corporate growth and competitiveness in the global economy. Mergers involves the consolidation of two entities where one transfers all its assets to the other entity which dissolves its existence. In contrast, an acquisition happens when one company

purchases the shares or assets of the target firm gaining full or partial control (Wang et. al, 2013). In today's world, mergers and acquisitions (M&A) have become a standard practice for companies that want to compete in the dynamic global landscape. Worldwide, M&A strategies are pursued in order to achieve competitive advantage through growth, consolidation, entry into new markets, and perceived financial gains. Despite their growing importance and popularity worldwide, M&A are least practiced among Ethiopian companies in general and the banking sector in particular (Girma, 2022). However, recent developments suggest that this is likely to change. The Ethiopian government has initiated significant reforms aimed at liberalizing and strengthening the financial sector.

While M&A is well-studied in global and developed market contexts, localized research in Ethiopia is scarce. The specific factors that may influence such decisions in emerging economies like Ethiopia remains poorly understood. Only a few studies have systematically examined what motivates M&A in Ethiopian banking industry, and how these dynamics align with broader national reforms. To mention few (Girma 2022 and Terefe 2022) have explored Bank consolidation from regulatory and motivation point of view. However, there is still a noticeable gap in academic research on the drivers, and implications of M&A in the Ethiopian banking sector post economic liberalization. Theories and drivers identified in other economies may not translate well to Ethiopia's unique context, where banks are often founded along ethnic, religious, or regional lines, adding a layer of complexity to consolidation efforts.

Taking into account the recent developments in the Ethiopian Financial sector, this study aims to identify the drivers of M&A decisions in Ethiopia's banking sector by gathering insights from senior management of selected private commercial banks, the research will offer insights and contribute to the limited body of knowledge on this topic. Ultimately, the findings will help inform policy-makers, regulators, and financial institutions as they navigate the complex transition toward a more robust and competitive banking system.

The research aims to address the following key questions:

1. What are the major factors that may drive M&A decision in the Ethiopian Banking Sector?
2. Does financial performance improvement drive M&A decisions?
3. Does the need for regulatory compliance influence M&A decisions?
4. Does the desire for market expansion influence M&A decisions?
5. Does diversification impact M&A decisions?
6. Does cost saving synergy drive M&A?
7. Does the need for better branding drive M&A?

8. Does the need for crisis driven survival influence M&A?

1.5 Objective of the Study

1.5.1 General Objective

The general objective of the study is to analyze factors that may drive Merger and Acquisition activity of Ethiopian Banks.

1.5.2 Specific Objective

- To assess the role of financial performance improvement in driving M&A.
- To examine how regulatory compliance influence M&A decisions.
- To analyze how the desire for market expansion influence M&A decisions.
- To analyze how diversification will impact M&A decisions.
- To examine cost-saving synergies as a driver of M&A
- To evaluate how branding can drive M&A decisions.
- To examine how crisis driven survival influence M&A

1.6 Delimitation and Limitations

This study is focused mainly to exploring the factors that may drive the Merger and Acquisition of Ethiopian Banks and will focus only on Management members of the private Commercial Banks in Ethiopia.

Data for the study was gathered from Executive and Senior Management at the banks, who have strategic decision-making responsibilities and are believed to have more expertise in the banking sector and the subject being studied. The outcome of the study entirely depends on the responses of respondents included in the study. Although Ethiopia's banking sector has a long history, the domestic banks have little or no experience on M&As. Historical data is not readily available. So in this case, the researcher relies on the view and perception of respondents in selected domestic banks. The data collection is based on the opinion of the respondents and this may give rise to bias due to the lack of objectivity. Moreover, the opinion of a person might change from time to time.

The study has included all medium sized banks (as per the classification on the second Financial Stability Report of NBE November 2024) and selected small banks that have operated on the market for 10 years or more. Additionally, the public banks Development bank of Ethiopia and Commercial Bank of Ethiopia are excluded due to their peculiar nature.

1.7 Significance of the Study

This study will provide a better understanding of the factors that will likely influence M&A activity in the Ethiopian banking sector and will inform stakeholders to make strategic decision in this regards.

Hence, is useful to financial institutions, policymakers, regulatory authorities, and bank management as it will inform them of the factors driving M & A which will facilitate informed decision making and policy formulation to promote sustainable growth and development of the Banking industry in Ethiopia.

The study can also be used by other researchers who want to study further in this or related areas as a reference or serve as a reading material for anyone who is interested. Finally, this research is expected to stimulate research interests among academics, and students to further investigate in the factors that will drive mergers and acquisitions in the Banking sector.

1.8 Organization of the Paper

Generally, the study comprises of five Chapters.

Chapter one gave a brief introduction about the study: including background of the study, statement of the problem, objectives, significance, delimitation and limitation of the study.

Chapter two presented review of related literature and gave a comprehensive discussion of Merger and Acquisitions and its driving factors.

Chapter three dealt with the research methodology employed in the execution of the study.

Chapter four focused on data analysis, interpretation and discussion of the data collected.

Finally, the summary of findings, conclusion and recommendation of the study was presented in Chapter five. It also addressed limitations and future research recommendations.

CHAPTER TWO

LITERATURE REVIEW

The literature reviewed in this part, focuses on the objectives stated in Chapter One. The value of studying the aforementioned literature areas is to provide a meaningful discussion and analysis about the topic. At the end of this section it is hoped that a critical understanding of key issues is exhibited, that the reader is better informed and that there is a clear justification for the research in this area.

2.1 Theoretical Review

2.1.1 Overview

Mergers and acquisitions (M&A) have become widely known strategies for organizational restructuring and growth (Gaughan, 2010; Terjesen, 2009). Though the terms are often used interchangeably, they refer to different processes and have distinction between them. A merger involves two or more companies coming together to form a new organization, typically on equal terms. In contrast, an acquisition occurs when one company takes control of another, either by purchasing it entirely or absorbing key parts of its operations (Terjesen, 2009).

While M&A activity has been a common trend in developed economies, particularly since the late 20th century, it has only more recently become a common practice in emerging economies. Today, many companies pursue mergers or acquisitions to strengthen their competitive position, expand their market presence, access new products or technologies, and broaden their customer base.

This trend is especially common in sectors such as manufacturing and financial services. The main motivations for M&A typically include the desire to increase market share, respond to regulatory or policy changes, reduce competition, realize business synergies, enter new markets, or acquire specific expertise or capabilities (Garrow & Holbeche, 2000; Pol, 2020).

2.1.2 Definition of Mergers and Acquisitions

- Merger: A merger happens when two or more companies combine and the acquiring company takes over the assets and liabilities of the other. While the acquiring firm may change significantly after the transaction, it typically retains its original identity.

- Acquisition: An acquisition involves one company purchasing the other in full or in part by purchasing a division, or production facility.

Although the difference in meaning between the two terms may seem minor, since the net result is often the same where two companies (or more) that had separate ownership are now operating together, the implication of each differs considerably especially in relation to the corporate strategy, taxation and even organizational culture.

Generally, a merger typically refers to two companies joining together (usually through the buying of shares) to become one. An acquisition on the other hand has one company i.e the buyer, that purchases the assets or shares of the seller, thorough payment made in the form of cash, the buyer's shares, or other valuable assets (Sherman and Hart, 2006).

2.1.3 Historical Evolution of Mergers and Acquisitions

The evolution of mergers and acquisitions (M&A) has historically followed distinct cyclical patterns, commonly referred to as waves (Clark & Mills, 2013). The first documented wave happened in the United States around 1891, primarily driven by firms seeking to establish monopolistic control, manipulate pricing structures, and eliminate competition. During this phase, the pursuit of economies of scale was not a central objective (Beckett, 1986; Lamoreaux, 1985).

The second wave of M&A that took place during the 1920s, reflected a shift in corporate strategy. Firms increasingly pursued economies of scale, aiming to grow more efficient through consolidation (Martynova & Renneboog, 2008). This period saw a transition away from monopolistic control toward the formation of oligopolies, as a few dominant players came to control major industries (Stigler, 1950).

The third wave occurred during the 1960s, largely influenced by the introduction of antitrust legislation in the United States designed to prevent monopolies and promote fair competition (Shleifer & Vishny, 1991). During this period, the strategic emphasis moved toward diversification with many firms acquiring firms in unrelated industries with the intention to enter new markets and develop autonomous business units. This approach aimed to reduce risk, enhance firm value and stabilize cash flow variability (Copeland, Weston, & Kuldeep, 2004).

The fourth wave of the 1980s, was characterized by globalization and increased capital mobility, which saw a rise in leveraged buyouts (Jewoo & Tianshu, 2014). Modifications in antitrust policy allowed for an increase in horizontal mergers, while corporate restructuring enabled firms to concentrate on core competencies through strategic acquisitions and divestitures (Andrade, Mitchell, & Stafford; Bhidé, 1990).

This period was notable for hostile takeovers and high-profile deals, such as Gulf Oil and Kraft (Cordeiro, 2014).

The fifth wave, spanning from 1993 to 2007, was characterized by record-breaking deal volumes and the global spread of M&A activity (Jewoo & Tianshu, 2014). In 2000 alone, more than 8,500 mergers were reported, with a total value surpassing \$1.7 trillion (Sikora, 2001). A significant development during this wave was the active participation of emerging-market firms, particularly from China, using cross-border M&A as a tool for international expansion (Martynova & Renneboog, 2008). This phase also aligned with the dot-com boom and the rise of complex financial products like subprime instruments, which added liquidity to the market (Clark & Mills, 2013). However, the trend of declining acquisition premiums reflected a more cautious view on synergy realization and long-term post-merger performance (Alexandridis, Mavrovitis, & Travlos, 2012).

Despite variations in motives and market dynamics across different M&A waves, the overall trend has been one of continued growth in deal activity. By 2016, the total value of completed M&A transactions reached an all-time high of \$3.7 trillion, with the energy, utilities, and tech sectors drawing the most attention from buyers (Thomson Reuters, 2017).

2.1.4 Types of Mergers and Acquisitions

Primarily, there are three types of M&A strategies i.e. horizontal, vertical, and conglomerate.

1. A Horizontal M&A strategy involves a target and an acquirer that are operating in the same industry. Here, the main motive is to reduce costs by spreading expenditures across a larger pool of outputs, which is also known as economies of scale. Merging with or acquiring a competitor can help the firm to strengthen its market power and profits. Horizontal mergers involve the consolidation of firms operating within the same industry, offering comparable products or services, and often sharing a similar customer and supplier base (Gaughan, 2010). According to Finkelstein (1997), such mergers are typically pursued to achieve operational efficiencies by leveraging economies of scale and scope, both at the level of production and across the broader organizational structure. Cowling K. (1980) stated that horizontal mergers constitute a significant proportion of overall merger activity, particularly prevalent in sectors such as banking.

These mergers generally result in the removal of a direct competitor, thereby expanding the acquiring firm's market share and increasing the overall concentration within the industry. Furthermore, they are

frequently employed as strategic tools to enhance a firm's bargaining power within its network of commercial relationships, thereby reinforcing its market position (Green M B., 1990).

By consolidating market players, horizontal mergers tend to diminish competition, leading to increased market dominance by a few large entities, which can give rise to monopolistic tendencies (Garrow & Holbeche, 2000).

2. Vertical mergers and acquisitions involve the combination of firms at different levels in the production or distribution chain. This type of integration is typically pursued to enhance internal management processes and streamline coordination throughout the supply chain, often resulting in gains associated with economies of scope (Berk & DeMarzo, 2019). In other words, vertical mergers are combinations of companies that have a buyer seller relationship or are symbiotically related. These mergers happen when organisations that are engaged in related functions but at different stages in the production process merge with each other (Scott, 2003; Gaughan, 2010). Vertical mergers can take place backwards or forwards of the actual value chain to expand a firm's control into allied product lines. This enables companies to increase their control over more sources of supply and distribution, for reasons of security (Berger and Demsetz, 1999). Backward integration is the acquisition or ownership of the company increased control over supply. On the other hand, forward integration refers to control over distributors and resellers which may include the purchase of a distribution system or developing such system internally.
3. Finally, conglomerate mergers and acquisitions involve the union of companies from entirely different or unrelated industries. These mergers are primarily driven by the goal of diversifying a company's operations (Berk & DeMarzo, 2019). Conglomerate mergers take place between companies producing unrelated goods or services operating. This type of merger occurs when firms are moving into different areas adding new products or services to their operations. This strategy allows businesses to expand into new markets or product lines beyond their core functions. According to Fairburn and Key (1989) conglomerate mergers take place when an industry is already concentrated and regulatory bodies restrict further significant horizontal consolidation.

2.1.5 Theories of Mergers and Acquisitions

The behavioral hypothesis of mergers and acquisitions are explained in detail in this section.

2.1.5.1 Neoclassical theory

Neoclassical theory, also known as the traditional view, defines the merger and acquisition activity based on the view of value maximization and assumes that markets are efficient. According to this theory, decisions about mergers and acquisitions (M&A) are mainly aimed at increasing shareholder value. This approach puts the interests of shareholders above those of company managers, suggesting that corporate actions should be guided by what benefits shareholders the most (Larsson & Wallenberg, 2002; Sarika & Vasantha, 2018).

According to neoclassical theory, the structure of an industry, including the number and size distribution of firms, is determined by fundamental factors such as technological developments, government policies, and the prevailing conditions of supply and demand. When substantial changes or external shocks occur in any of these areas, they are likely to trigger corresponding shifts in the industry's structural configuration. As Baniya and Shah (2016) asserted, neoclassical theory is one of the important tool in predicting the merger and acquisition activities.

Neoclassical theory posits that managerial decisions are driven by the objective of maximizing profits or enhancing shareholder value, with mergers serving as a means to either improve operational efficiency or strengthen market power (Gugler et al., 2005). From this perspective, mergers are also viewed as mechanisms for reallocating resources between efficient and inefficient firms in response to industry-level shocks. This view supports the notion that merger waves tend to emerge in sectors undergoing fundamental transformations (Harford, 2005; Andrade & Stafford, 2004; Jovanovic & Rousseau, 2002). As noted by Brealey et al. (2008), a merger is considered value-creating when the combined entity is worth more than the sum of the individual firms operating separately.

2.1.5.2 Behavioral Theory

Behavioral theory assumes that mergers and acquisitions happen due to overvalued markets and managerial timing. The theory focuses more on the correlation between merger and stock market valuation. It suggests that managers often pursue mergers when their firm's stock is overpriced, believing they can time the market to their advantage (Eckbo, 2010). Overconfident CEOs, in particular, are more likely to engage in acquisitions—especially those unlikely to create value—because they overestimate their ability to generate synergies (Malmendier & Tate, 2005).

This theory also introduces the concept of hubris, where executives overpay for targets due to excessive optimism or inflated self-belief (DePamphilis, 2008). Biases like herding, anchoring, and overcommitment further influence M&A decisions, often leading to value-destroying deals. In summary, behavioral theory highlights how overconfident managers and market misjudgments play a central role in driving merger activity that are value destroying.

2.1.5.3 Agency Theory

Agency theory explains how conflicts of interest between managers and shareholders can influence merger decisions. Even when managers act rationally, they may prioritize personal goals—such as increasing compensation, expanding control, or securing job stability—over shareholder value. These agency problems often arise when managers hold little ownership in the firm, creating misalignment with shareholders. Low stock prices put pressure on managers to take actions to raise the share price or become the target of the acquirers, who perceive the stock to be undervalued (Fama & Jensen, 1983).

Mergers can result from such conflicts, especially when managers seek to use excess cash or undervalued stock for their own benefit (Mehran & Peristiani, 2010). In some cases, acquisitions are pursued not for synergies, but to grow the company and enhance managerial power or prestige (Masulis, Wand & Xie, 2007). Agency theory thus emphasizes that M&A decisions may be driven by personal incentives rather than the best interests of the firm's owners.

Agency theory assumes that managers, acting in their own self-interest, may use their access to superior information to pursue actions that benefit them personally. This includes strategic moves like expanding market presence or enhancing the company's brand—often through mergers and acquisitions—not solely for the firm's benefit, but also to gain private advantages (Baniya & Shah, 2016). Ultimately, such mergers, while rational from the manager's perspective, can result in destroying value rather than achieving the expected synergies.

2.1.5.4 Resource Dependence Theory

Resource Dependence Theory emphasizes that organizations are influenced by their need to access and control critical external resources for survival. To reduce uncertainty and gain autonomy, firms often seek strategies that internalize these dependencies. Mergers and acquisitions are a key method for managing such external constraints, allowing firms to secure vital inputs and reduce reliance on outside entities (Pfeffer &

Salancik, 1978; Vanhaverbeke et al., 2002). Inter-organizational interdependencies are recognized as a major factor driving mergers and acquisitions, as acquiring a key resource provider can ensure stable access to inputs, enhance organizational knowledge, and support coordinated strategic efforts (Meyer et al., 2009). While M&A is a common solution, businesses also turn to alternatives like partnerships, board connections, and joint ventures to handle these interdependencies (Dussauge et al., 2000; Ellstrand et al., 2002; Pfeffer & Nowak, 1976).

2.1.6 Motives for Mergers and Acquisitions in the Banking Sector

Firms undertake M&A for many reasons usually determined according to their strategic objectives. The rationale behind mergers and acquisitions (M&As) is shaped by a combination of strategic and financial considerations. A common motivation found across the literature is the pursuit of corporate growth and diversification (Coyle, 2000; Paulter, 2001; Stahl & Mendenhall, 2005). Revenue enhancement is another frequently cited driver (Huang & Kleiner, 2004), particularly in industries facing intense competition or economic shifts (Bruner, 2004; Croson et al., 2004). Firms may also use M&As to gain access to new knowledge or capabilities, enhancing their learning potential (Blonigen & Taylor, 2000; Ghoshal, 1987), or to acquire valuable resources such as talent, intellectual property, or infrastructure (Barney, 1991). Cost reduction through economies of scale remains a critical driver (Coyle, 2000; Paulter, 2001; Walter & Barney, 1990), while enhancing market power and competitive position is another significant factor (Trautwein, 1990).

Several scholars differentiate between the motivations for mergers and those for acquisitions. Mergers are often viewed as a strategic means for entering new markets, developing new products, and increasing operational efficiency (Gaughan, 1999; McClure, 2010; Sherman & Hart, 2006). Additional benefits may include technical improvements, better management performance, tax advantages, and effective utilization of surplus capital (Fontaine, 2007; Paulter, 2001; Sherman & Hart, 2006). Mergers can also generate synergies, producing greater combined value than the individual firms could achieve alone (Cigola & Modesti, 2008; Gaughan, 1999).

On the other hand, acquisitions are frequently aimed at achieving scale efficiencies, gaining market dominance, or accessing superior technologies (Miller, 2008; Sherman & Hart, 2006; William, 2009). They can also provide entry into new product lines or geographical markets and reduce the number of competitors (Coyle, 2000; Fontaine, 2007; Miller, 2008). Overall, the literature suggests that M&As are complex

strategic choices influenced by internal ambitions and external forces. They offer firms opportunities to strengthen their competitive positions, enhance efficiency, and support long-term growth.

While earlier studies often separated the motives for mergers from those for acquisitions, recent scholarship suggests a need for a more integrated framework. One proposed approach is to classify M&A motives into internal and external categories, drawing from psychological theories of motivation. Internal motives usually include the desire to grow, increase revenue, increase financial position, develop new products/services, increase market position, increase management efficiency, increase shareholder's equity/capital, achieve higher efficiency, improve technical competency, etc. External motives arise from bank's environment and may further be divided into four categories: economic, legal-political, technological and competitive.

In sum, the literature suggests that M&As in banking are rarely driven by a single factor. Rather, they reflect a complex interplay of internal strategies and external pressures. This dual-framework approach not only unifies previous research but also provides a useful basis for future theoretical and empirical investigation.

As indicated earlier, Literature review has identified various possible factors that drive mergers and acquisitions. The ensuing table illustrates the list of factors contributing to mergers and acquisition decisions according to the works of Smirnova (2014);

Table 1: Summary of Literature Review: Factors Driving M&A

Factors driving M&A	Author/s
- to enter into new markets, to develop new products and/or services	Walter and Barney (1990); Gaughan (1999); Bower (2002); Sherman and Hart (2006); McClure (2010)
- to exploit strategic opportunities through synergies and convergence of industries	Gaughan (1999); Coyle (2000); Bower (2002); Miller (2008); Cigola and Modesti (2008)
- to reduce the number of competitors	Sherman and Hart (2006); Fontaine (2007)
- to ensure corporate growth and diversification	Walter and Barney (1990); Coyle (2000); Paulter (2001); Stahl and Mendenhall (2005)
- to obtain revenue growth	Coyle (2000); Huang and Kleiner (2004)
- to improve technical competency and increase efficiency of management	Gaughan (1999)
- to acquire R&D capability	Bower (2002)
- to enhance learning, obtain new knowledge, combine superior technology	Ghoshal (1987); Blonigen and Taylor (2000); William (2009)

- to gain access to better and greater resources	Barney (1991); Coyle (2000); Miller (2008)
- to achieve greater efficiency through economies of scale	Walter and Barney (1990); Gaughan (1999); Coyle (2000); Paulter (2001); Sherman and Hart (2006); Fontaine (2007); Miller (2008); William (2009); McClure (2010)
- to increase market power	Trautwein (1990); Paulter (2001); Miller (2008)
- to respond to changing economic conditions	Coyle (2000); Croson et al (2004); Bruner (2004)

Source: Smirnova (2014)

Moreover, the following table illustrates the list of factors contributing to mergers and acquisition decisions specifically to the Banking Industry according to the works of Smirnova (2014);

Table 2: Summary of Literature Review: Factors Driving M&A in the Banking Sector

Factors driving M&A	Author/s
- to achieve efficiency through economies of scale	Focarelli et al (2002); Humphrey and Vale (2003); Pasiouras and Zopounidis (2008); Sufian (2011)
- to grow, increase size and strengthen market position	Morris (2004); Pasiouras and Zopounidis (2008); Kingston University (2007)
- to get higher income by selling more services to a greater set of customers	Focarelli et al (2002)
- to improve the quality and diversify portfolio	Focarelli et al (2002)
- to get easier access to international money and capital markets	Pasiouras and Zopounidis (2008)
- to respond to the changing economic conditions in a bank's environment	Morris (2004)

Source: Smirnova (2014)

2.1.7 Empirical Evidence on Mergers and Acquisitions

An enormous body of research has been conducted on bank mergers and acquisitions in different countries. These empirical studies across the countries reveal that M&A decisions are shaped by various factors such as internal organizational characteristics, external economic conditions, strategic goals, and regulatory environments.

Boyd and Graham (2000) examined U.S. banking M&A activity during consolidation waves and found that market-driven forces such as increased competition and economic instability were primary triggers. M&As were often used to prevent further collapse of institutions during financial downturns, with regulatory support reinforcing these trends. While Morris (2004), asserted that the long history of M&A activity in the United States was largely due to the weakness of small banks that led to consolidation as a means of survival.

In Brazil, a recent study using employer-employee data (2003–2017) revealed that M&As were often motivated by the need for firms to strengthen market power and remain competitive in high market competition. The evidence identifies that even without labor market monopolization, M&As helped firms to adjust employment arrangements so as to stay competitive (Galle et al., 2023).

Pfeffer and Salancik (2003) noted that M&As are utilized to mitigate uncertainty in volatile environments. Merger with a competitor or larger firm allows firms to pool resources, reduce risk, and maintain operations during financial crisis. This was observed during the 2008 global financial crisis when banking mergers were intentionally supported to prevent systemic failure.

A study on consolidations in Ghana's banks indicated that bank distress compelled some of the weak and undercapitalized banks to consolidate or be acquired. The central bank encouraged such actions to increase liquidity and operational efficiency (Abor & Adjasi, 2007).

M&As have a tendency to give access to better brand equity. Sheen (2015) determined that in the U.S. consumer goods sector, convergence of brand quality using M&A had an impact on customer loyalty and enhanced post-merger brand perception. Companies were able to build on the reputation of acquired brands to strengthen their market position. Baniah and Shah (2016) argued that for banks in emerging markets, building a strong brand independently is resource-intensive. M&As enables to improve brand image and credibility by leveraging the acquired firm's brand capital.

According to Boyd & Graham (2000) regulatory frameworks significantly influence M&A activity. For example, the U.S. government played an active role in facilitating bank mergers during economic downturns to stabilize the financial system.

Hardlock et al. (1999) found that banks with higher levels of managerial ownership were less likely to be acquired. This suggests that managers with substantial ownership stakes may resist M&A attempts to maintain control, especially if mergers threaten their influence or strategic vision.

After studying multiple of factors that affect M&A in Nepal banks only four factors were found significant influencers as motives of M&A activities. These factors include emphasis providing service, emphasis on cost efficiency, emphasis on better branding and fulfilling capital requirement (Baniya & Shah, 2016).

Efficiency is another key factor behind M&A activities. Humphrey and Vale (2004) emphasized the importance of using advanced cost function models to accurately measure potential economies of scale and cost savings. Their research found that, on average, banks anticipated cost reductions following mergers. Many institutions even developed specific “checklists” to guide their post-merger integration strategies and identify cost-saving opportunities.

In Korea, Sufian (2011) examined the post-merger efficiency of banks, while in Malaysia, Shanmugam (2003) found that M&As were largely motivated by the need to enhance efficiency and competitiveness. Pasiouras and Zopounidis (2008) reported that Greek banks pursued M&As to grow in size and gain easier access to international capital markets. Similarly, Focarelli et al. (2002) observed that Italian banks were focused on increasing non-interest income and optimizing capital use through mergers.

Aston and Karamanova (2009) examined Kazakhstan’s banking sector and found that M&A activity occurred in two distinct waves. The first wave, in the mid-1990s, was driven by government-led restructuring and privatization while the second wave, in the late 2000s, due to foreign banks entry to Kazakhstan. Following the global financial crisis, the government initiated a nationalization process to stabilize failing institutions, highlighting both internal and external motivations for M&A.

In developed countries, bank mergers and acquisitions are largely shaped by market dynamics such as competition and strategic growth. However, in many developing nations, it is often the regulatory authorities that drive M&A activity. In these settings, especially during financial crises, mergers serve as a way for struggling banks to exit the market under the guidance of central banks or financial regulators. A clear example is case of Lebanon in the 1980s. After deregulation led to a surge in small, poorly capitalized banks, the government intervened to stabilize the sector by tightening capital requirements and restricting new branch openings to just two per year, the authorities effectively pushed smaller banks toward merging with larger institutions. These efforts led to 25 formal bank mergers between 1994 and 2002. Morris (2004) emphasized that evolving social and regulatory frameworks in the banking sector influenced M&A activities over time. Likewise, Pilloff (2004), in his study on U.S. banks, highlighted how the loosening of geographic restrictions and advances in information technology served as critical catalysts for merger activity.

Developed countries have a well matured M&A process and well documented history of M&A. Hence, there are ample bodies of research on factors motivating M&A in those economies. In Ethiopia, the practice of merger and acquisition is very limited. However, recently there have been various economic developments such as capital requirement and liberalization of the Banking sector that are pushing the Banking industry towards M&A. Hence, it is imperative to study the factors that may trigger mergers and acquisitions.

2.1.8 M&A in African Banking: Contextual Gaps in Ethiopia

Mergers and acquisitions (M&A) have become significant strategies in the African banking sector, driven by various factors such as regulatory reforms, market competition, and the pursuit of operational efficiencies. Empirical studies have highlighted several key drivers of M&A activities across the continent. In countries like Nigeria, regulatory reforms, including increased minimum capital requirements, have prompted banks to consolidate to meet new standards. For instance, the Central Bank of Nigeria's 2004 consolidation policy led to a significant reduction in the number of banks through mergers and acquisitions, aiming to strengthen the banking sector's stability and competitiveness (Sanusi, 2011). Similarly, in Kenya, market-driven consolidations have been encouraged by both increased competition and stricter capital requirements, with notable mergers such as National Industrial Credit Bank and Commercial Bank of Africa driven by the need to expand scale and compliance (Ndung'u, 2017).

The liberalization of financial markets has exposed banks to increased competition, both domestically and internationally. Studies indicate that cross-border M&A activities are often driven by the desire for market expansion and the need to achieve economies of scale to remain competitive (Agbloyor et al., 2012).

Banks pursue M&A to realize operational efficiencies and synergies, such as cost reductions and enhanced service offerings. Research in Ethiopia suggests that large private banks are more likely to achieve efficiency gains through M&A, primarily due to learning effects rather than resource complementarity among merging units (Bayiley & Redae, 2022).

Ethiopia presents unique challenges and opportunities regarding M&A in the banking sector. The Country's financial sector has been less developed compared to other African countries, with limited foreign investment and a lack of a formal stock exchange, which affects the dynamics of M&A activities (Tessema, 2023).

Furthermore, recent legislative changes, such as the 2024 Banking Business Proclamation permitting foreign banks to establish subsidiaries and acquire shares in local banks, may alter the M&A landscape by introducing new competitive pressures and opportunities for consolidation. However, some of the

challenges of M&A in the Ethiopian context include lack of experience, regulatory challenges, possible management resistance and most of all ethnic based affiliations and establishment of most of the banks. Addressing these contextual gaps requires tailored research that considers Ethiopia's specific economic, regulatory, and institutional environments. Understanding the unique factors influencing M&A decisions in Ethiopia is crucial for policymakers and banking institutions aiming to navigate the evolving financial landscape.

2.2 Conceptual Framework and Hypothesis

This section of the research paper gives a description of the way the research framework was formulated. It is mainly derived from main findings of other researchers' studies like Baniya and Shah (2016), Smirnova (2014), Gallo G. (2023) and so on.

The research has employed the neoclassical, agency, behavioral and resource dependency theories to analyze the determinants of merger and acquisition in the Ethiopian Private Banks. The private banks are presumed to be willing to undertake merger and acquisition activity (dependent variable) as a result of one or more of the determinants of M&A (the independent variables). The independent variables used in the conceptual model are financial performance enhancement, adherence to regulatory necessities, market growth, diversification, cost reduction, branding, and survival.

2.2.1 Independent Variables

The independent variables consist of various factors that are considered to drive general merger and acquisition decisions and factors that are specific to the banking industry, which are described hereunder;

i. Financial Performance Improvement

Financial performance improvement can be considered as a determinant which influences M&A decision in the Private Banks of Ethiopia. Financial improvement in the banking sector involves enhancing the overall financial health, typically through a set of parameters like profit margins, income growth, liquidity levels, and capitalization. The principal objective of such improvements is to achieve optimum shareholders' returns while developing a more robust and sustainable operational framework. Gaughan (2018) continues that in addition to revenue growth mergers and acquisitions will also result in improved profitability on account of synergistic gains. This point has been argued by Weber et al. (2013) that if two or more firms

operating in the same or related lines of business have synergy, then it is more lucrative to run the two firms together rather than separately.

Hypothesis 1: There is positive relationship between financial performance improvement and merger and acquisitions decision.

ii. Compliance with regulatory requirement

Regulatory compliance in the financial sector refers to the capacity of a financial institution to comply with and operate in the framework of laws and regulations issued by governmental and regulatory bodies, e.g., the central bank, financial market authorities, or other supervisory agencies (Gallo G., 2021). These encompass adherence to standards and policy directives such as minimum paid up capital requirement Directive SBB-78-2021 which revised the minimum paid up capital requirement to 5 billion birr with the time frame to raise the capital within five years (2026) from the passing date, capital adequacy requirement (the NBE strategic plan is to adopt Basel II/III framework by June 2025), and other financial and operational requirements. Besides, if the regulating body, i.e. NBE, initiate forced/statutory merger then banks will be forced to comply.

Hypothesis 2: There is positive relationship between compliance with regulatory requirement and merger and acquisitions decision.

iii. Market expansion

The banking industry is increasingly competitive, with new entrants entering the market and established banks wanting to enhance their market share. M&As provide opportunity for banks to expand their reach and market share quickly. Mergers and acquisitions are often pursued as strategic tools to reduce market competition and expand an organization's share within the industry. According to Reaund (2016), such transactions can significantly enhance a company's market presence and competitive standing. By consolidating with or acquiring other firms, companies aim to strengthen their market position and scale up operations to gain a larger portion of the market.

Hypothesis 3: There is positive relationship between market expansion and merger and acquisitions decision.

iv. Diversification

Diversification is yet another M&A driver. It follows an assumption that companies can attain their optimal level of risk in case they invest across various financial assets (Motis, 2007). Diversification is a corporate concept applied by companies in mitigating firm-specific risks through the diversification of the sources of revenue along with operations into various fields. Verma and Sharma (2014) corroborate that mergers and acquisitions are regularly a way for firms to enter into new markets, thereby diversifying and restructuring their business. Further, diversification enables companies to more effectively utilize their resources by transferring funds from sections of the business in which there is surplus capital to other areas where the funds would be more effective (Okafor, 2018).

Hypothesis 4: There is positive relationship between diversification and merger and acquisitions decision.

v. Cost Saving

Banks are able to realize cost saving through rationalization of operations, eliminating excess staff, centralization of operations, and cutting down unnecessary costs. The cost saving is particularly necessary in the case of mergers and acquisitions (M&As). When two banks merge, they become efficient by conducting operations on a greater scale. The result can be reduced expenditure in areas such as procurement, advertising, and technology since the combined entity is able to share resources and avoid duplication (Gallo, 2023).

Hypothesis 5: There is positive relationship between cost saving and merger and acquisitions decision.

vi. Branding

In case of mergers and acquisitions, the pursuit of better brand positioning is an important driving factor. Banks may engage in merger and acquisition to acquire a well-established brand with favorable market reputation.

Baniah and Shah (2016) highlight that building a strong brand typically requires significant time and investment. In this context, mergers and acquisitions can provide banks with a faster and more efficient way to improve their brand image, with less activity than had it been done independently. Sheen (2015) supports this view, noting that when two competing banks come together, their brand qualities often merge as well. This blending of brand identities can shape how customers perceive the new entity, often leading to a stronger, more unified brand presence in the market. Novickyte and Predroja (2015) argue that branding is one of the factors affecting merger and acquisition decision.

Hypothesis 6: There is positive relationship between branding and merger and acquisitions decision.

vii. Survival

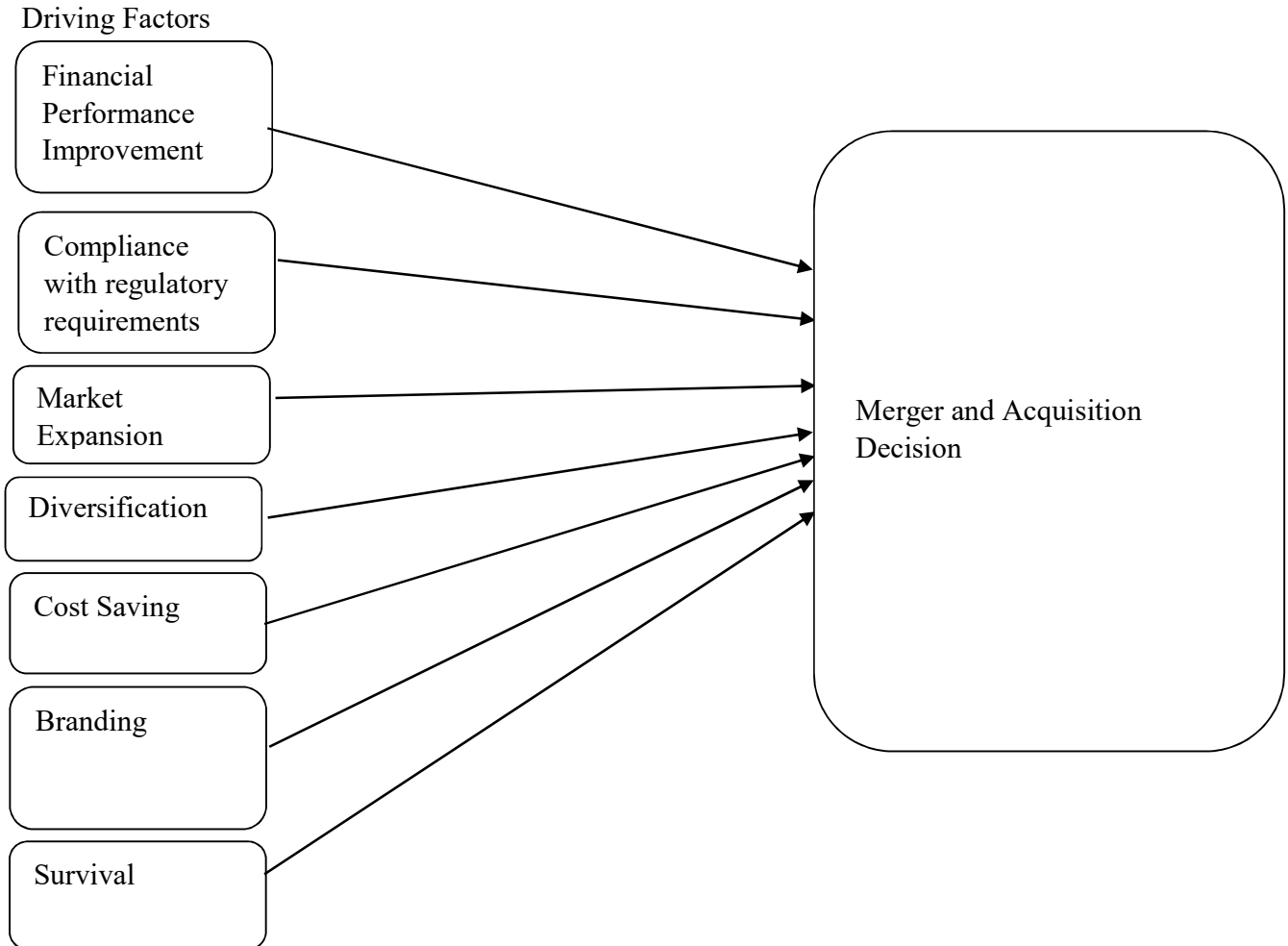
Mergers and acquisitions (M&As) can be a survival strategic response of banks exposed to challenging macroeconomic conditions, heightened competition, or financial distress. Under these circumstances, M&As can serve as a survival mechanism, allowing institutions to stabilize and remain in business instead of facing institutional failure. One of the most notable arguments for mergers by firms within same industry, according to Pfeffer and Salancik (2003), is the elimination of uncertainty caused by competitive pressure. Similarly, Boyd and Graham (2000) observed that M&A waves in the United States were largely driven by market dynamics, with mergers seen as a practical solution to prevent the failure of more financial institutions. They also emphasize the important role of regulatory authorities, in driving statutory mergers as a means to safeguard the stability of the banking sector and mitigate failure.

Hypothesis 7: There is positive relationship between survival and merger and acquisitions decision.

2.2.2 Dependent Variable

The dependent variable in this case is the decision to go for merger and acquisition as a result of the various driving factors. The banks would decide to perform merger and acquisition activities if they consider the various influencing factors.

Figure 1: Conceptual Framework designed by the researcher



The general form of the model is as follows:

$$M\&A = \beta_0 + \beta_1 \text{FinancialPerformance} + \beta_2 \text{Compliance} + \beta_3 \text{Mkt Expansion} + \beta_4 \text{Diversification} + \beta_5 \text{Costsaving} + \beta_6 \text{Branding} + \beta_7 \text{Survival}$$

Where, M&A= Mergers and Acquisition, and β_0 is constant, β_1 , β_2 , β_3 , β_4 , β_5 , β_6 and β_7 are coefficient to estimate.

CHAPTER THREE

RESEARCH METHODOLOGY

In this chapter the methods used in the thesis paper are discussed. The chapter describes the detailed research methodology that is adopted to address issues identified earlier, together with the means of collecting data for analysis, and the analysis approach.

3.1 Research Design

This study adopted an explanatory research design in order to examine the causal relationships between various driving factors and merger and acquisition (M&A) decisions in the Ethiopian commercial banking sector. Explanatory research is suitable when the objective is to identify the underlying causes of a phenomenon and to test hypotheses about the relationships between variables. Unlike exploratory research, which focuses on discovering new insights, explanatory research is designed to provide evidence-based explanations, making it appropriate for this study which seeks to determine the extent to which specific motives influence M&A decisions. The type of research was a cross-sectional research survey in which the collection of information from the respondents was carried out at a single-point in time.

The research employed quantitative approach. This approach is particularly relevant in studies where patterns, relationships, and impacts of multiple variables need to be assessed rigorously. The quantitative approach involved administering structured questionnaire to a sample of Senior Management members from selected commercial banks in Ethiopia. The survey questionnaire was developed to assess the driving factors towards M&A activities.

3.2 Population of the study

The study considered private commercial banks in Ethiopia, which started operations atleast a decade ago or before 2014. Small banks that have only been recently established and haven't yet operated in the market for long have been excluded from the study. The reason for exclusions is because their strategies and operations may still be evolving, making it difficult to attribute their behavior to the same factors affecting more established banks. Moreover, including new banks might skew the results because their M&A motivations can be very different from the more matured ones. At the end of 2014 fiscal year, there were 19 banks (16 private and 3 public). Therefore, the target population of this study comprises of 16 private commercial banks. The study excludes state owned banks due to their distinct nature as government policy instruments.

Unlike private banks, they are not primarily market-driven and typically enjoy stronger capitalization and decisions are guided more by national development objectives than competitive or financial pressures.

The target respondents of the survey are Senior Management Members consisting of Presidents, Vice Presidents, and Department Directors who are able to provide information on factors driving mergers and acquisitions. The 16 private Banks have in total 658 management employees comprising of 143 Executive Management and 515 Senior Management members. Hence, the target population of the study is 243 applying the sampling formula shown below with confidence level of 95% and 5% confidence interval.

$$\text{To calculate the sample size } n = \frac{z^2 * p * (1-p)}{E^2}$$

Apply finite population correction

$$N = \frac{n}{1 + (n-1/N)}$$

Hence the sample size is 243.

Table 3: Number of Senior Management in the Private Banks as at September 2024

No.	Banks	No. of Chief Officers/VP	No. Directors	Sum	%age share of sample size
1	Awash	18	57	75	28
2	DB	14	61	75	28
3	BoA	14	48	62	23
4	WB	3	38	41	15
5	HB	4	31	35	13
6	NIB	12	37	49	18
7	CBO	12	57	69	25
8	LIB	7	26	33	12
9	OB	12	22	34	13
10	ZB	7	29	36	13
11	Bunna	6	17	23	8
12	Berhan	10	27	37	14
13	Abay	11	19	30	11

14	AdIB	4	12	16	6
15	GBE	4	16	20	7
16	EB	5	18	23	8
	Total	143	515	658	243

3.3 Sampling Procedure

Sampling provides a range of techniques that facilitate to reduce the amount of data needed to collect by considering only data from a sub group rather than all possible cases or elements. In this study, proportional stratified random sampling technique was used in order to get proportional representative sample from management employees of private banks in Ethiopia. The management members are taken as target population because they are directly involved in the strategic decision-making processes surrounding mergers and acquisitions. Their insights are critical to understanding the key factors that influence such corporate action.

According to Kelly and Bland (1998) the technique produce estimate of overall population parameters with greater precision and ensures a more representative sample is derived from a relatively homogenous population. The study grouped the population into two strata Executive Management and Senior Management. According to Cooper and Schindler (2003), random sampling frequently minimizes the sampling error in the population. Stratified random sampling was used since the population of interest can be subdivided into groups or strata.

3.4 Types and Sources of Data

In research, data is the foundation upon which analysis and conclusions are built. Data types are classified into two main types primary and secondary data.

Primary data refers to information collected directly by the researcher for the specific purpose of the study. This type of data is original and firsthand, gathered through methods such as questionnaires, interviews, observations, or experiments. The main advantage of primary data is its relevance and specificity to the research objectives, which allows for greater accuracy and control over the quality of information collected. In this study, data was collected by using primary sources of data. Primary data was important for this study and was gathered through a set of self-administered structured questionnaire.

3.5 Methods of Data Collection

Data collection is the process of gathering and measuring information on variables of interest, in a systematic way that enables one to answer defined research problems, test hypothesis and evaluate outcomes. Questionnaire is the most commonly used method in surveys. It is the list of questions either open-ended or close-ended for which the respondents provide answers in written form. A questionnaire may be prepared with questions that measure separate variables or with questions that are aggregated into a scale. A questionnaire designed with questions in a scale form are used for tests (Kabir, 2018).

Data was collected from primary sources of data through questionnaire. The measurement used for the close ended questions in the questionnaire is the Likert Scale. It consists of statements where respondents indicate their degree of agreement or disagreement on a five-point scale: Strongly Disagree, Disagree, Neutral, Agree, and Strongly Agree.

3.4.1 Structure of the Questionnaire

The final design of the questionnaire included three parts (Annex to be attached). Within each section complete instructions and guidance are provided to respondents on how to answer the section.

For the second and the third parts of the questionnaire, respondents are asked to select their level of agreement or disagreement on each statement included in the section by using a five point Likert scale ranging from “Strongly disagree” to “Strongly agree”. The questions for each variable are adopted from various sources with some modifications.

Part I: Profile of the Respondents

The first part of the questionnaire was concerned with obtaining some demographic data about the respondents to present the research respondents’ characteristics. There were four questions asking respondents about their gender, age, educational level and number of years of experience in managerial position.

Part II: M&A Related Issues

This part was concerned with investigating the M&A decision drivers. This section was divided into seven subsections as follows:

Subsection One: Financial Performance Improvement Related Questions

This part was concerned with strategic issues related to financial performance improvement. There are four statements measuring this variable which included increasing revenue; minimize volatility of

earnings; increase net interest income; increase operational and financial efficiency. This part of the questionnaire was adopted from Baniya and Shah (2016) and Terefe (2022).

Subsection Two: Compliance with regulatory requirements Related Questions

In this subsection, issues concerning regulatory compliance are included. There are five statements measuring this variable such as the paid up capital increase requirement, deadline to meet capital requirement criteria, allowing foreign banks to enter market, forced merger by regulator and change in BASEL regulatory standard. The questions in this part were adopted from Baniya and Shah (2016) and Terefe (2022).

Subsection Three: Market Expansion Related Questions

This part of the questionnaire was concerned with investigating the impact of market expansion on M&A decisions. Five statements including obtain power to exclude rivals, to capture better market share, to increase market power, to execute expansion strategy, and to access new market and customer segments were stated. The source used for this part was from Baniya and Shah (2016) and Terefe (2022).

Subsection Four: Diversification Related Questions

This part was concerned with issues related to diversification. There are five statements measuring this variable which included to offer wide range of products and services, to provide diversification of funding sources, to achieve geographic diversification, to diversify loan portfolio and to diversify risks. Questions were adopted from Baniya and Shah (2016) and Terefe (2022).

Subsection Five: Cost Saving Related Questions

There were five statements measuring issues in relation to cost saving including to minimize duplication of banking activities and processes, to achieve economies of scale, to provide access to better technology, to create synergy from shared services, and to increase production. Questions were adopted from Baniya and Shah (2016) and Terefe (2022).

Subsection Six: Branding Related Questions

In this subsection, issues concerning branding are included. There are five statements measuring this variable such as increase the positioning of banks, improve image of banks, obtain better branding, create better brand with less cost and increase the outreach of advertisements. The questions in this part were adopted from Baniya and Shah (2016) and Terefe (2022).

Subsection Seven: Survival Related Questions

This part of the questionnaire was concerned with survival related issues. Five statements were used to measure this variable including mitigate financial distress, withstand competition, existential threat from new entrants, security from environmental and macroeconomic factors and survive harsh economic conditions. The source used for this part was from Baniya and Shah (2016) and Terefe (2022).

Part III: M&A Decision related Issues

This part was concerned with investigating the M&A decisions of the Banks. Respondents were asked to give their agreement or disagreement in relation to M&A decision. This variable was measured by six set of questions. This part was adopted from Baniya and Shah (2016) and Terefe (2022).

3.6 Validity and Reliability of Instruments

To ensure the study effectively achieves its intended objectives, the researcher has checked the validity and reliability of the instrument of data collection during proposal stage before distributing the final questionnaires to the respondents. Validity is concerned with the extent to which an instrument measures what it is supposed to measure (Kothari, 2004).

Reliability refers to the extent to which a variable or a set of variables is consistent in measuring what it is intended to measure across various population and different period of time (Hair et al., 2007). According to Hair (2007), reliability is an assessment of the consistency between measurements that have one latent construct in common. One of the best methods for measuring such reliability when using the Likert scale is the Cronbach's alpha, the value of which falls into the range of 0-1 with measure towards 0 referring to the test becoming unreliable and the measure towards 1 referring to the test becoming reliable.

To ensure high validity and reliability of the data the researcher has taken a sample of 10% (22 respondents) of the population for the pilot study. The objective of the pilot study was to test whether the survey instrument provided consistent and accurate information so that the researcher identifies and amends problematic questions and refines the questionnaire to maximize response.

Cronbach's Alpha (α) was used as the measure for assessing internal consistency. Alpha values range from 0 to 1, with higher values indicating greater reliability. As suggested by Cronbach (1951) and supported by

Gliem & Gliem (2003), an α coefficient of 0.70 or higher is generally considered acceptable in social science research.

A total of eight variables comprising of 40 items were tested.

Table 4: Reliability analysis of variables

Items	Coefficients (Alpha)
M&A can be pursued for increased revenue by combining customer bases and product offerings.	0.915
M&A can help minimize the volatility of earnings of the merging banks.	0.914
Merger and acquisition may increase the net interest income (difference in revenue resulting from bank's assets and expenses associated with paying)of banks.	0.914
M&As may lead to increased operational and financial efficiency through the consolidation of processes and systems.	0.913
M&A may occur if banks are not able to meet the paid-up capital increase requirement set by the National Bank of Ethiopia (NBE).	0.913
M&A could take place among banks having trouble with meeting the deadline set to meet the capital requirement criteria.	0.914
M&A may occur between local banks as foreign banks are now allowed to operate in the country.	0.912
Banks may be forced to merge by the regulator (statutory merger) to bring efficiency and effectiveness among the banks.	0.913
Change in banking regulation standard, i.e. a shift from the current Basel I standard to advanced ones, can lead to M&A of banks.	0.912
In order to obtain power to exclude rivals, banks go through merger and acquisition.	0.912
Merger and acquisition have roles to capture better market share.	0.912
Merger and acquisition are used to increase market power when the bank acquires another bank in different	0.911
Merger and acquisition is an effective tool to execute expansion strategy of banks.	0.912
Merger and acquisition can provide banks with access to new markets and customer segments, leading to increased	0.912

In order to diversify and offer wider range of products/services to the customers, merger and acquisition is done.	0.911
M&A is done to provide diversification of funding sources, as the merged entity can have access to a wider range of funding options and capital sources.	0.911
In order to achieve geographic diversification, merger is done with banks having deeper market penetration and broader reach.	0.913
M&A is done to provide diversification of the loan portfolio, as the merged entity can benefit from a more diverse range of loan products and customer segments.	0.912
As part of related diversification, M&A can be performed to minimize and diversify risk in the market.	0.913
Merger and acquisition can help to minimize the duplication of banking activities, processes and systems through consolidation of operations.	0.913
In order to achieve economies of scale M&A can be done, as the merged entity can benefit from lower costs associated with larger scale operations.	0.912
M&A will provide access to better technology, which can improve operational efficiency and reduce costs.	0.913
M&A can be done to create synergies from shared services, as the merged entity can benefit from the consolidation of functions such as finance, Marketing, HR, Services and IT.	0.914
In order to produce more without increasing the individual capacity of banks, merger and acquisition is performed.	0.914
Merger and acquisition is done to increase the positioning of banks in the mind of the customers.	0.911
Merger and acquisition makes it possible to improve image of banks with less activities to be performed than had they done individually.	0.911
Merger and acquisition helps to obtain better branding of banks within short span of time.	0.913
Merger and acquisition helps to create the brand of banks with involvement of less cost than had it been done individually.	0.912
Merger and acquisition makes it easy for the advertisement of banks to reach to large number of consumers than had it been done alone.	0.911
M&A can be pursued as a survival strategy to mitigate financial distress and reduce the probability of bank failure.	0.912

M&A can be done to withstand the competition and gain competitive advantage in the market.	0.911
New entrants to the sector may pose existential threat for the existing smaller banks and hence lead them to M&A decision.	0.911
Merger and acquisition will make banks secure from various environmental factors such as economic, political, socio-cultural as well as technological factors.	0.911
M&A can help banks to survive during harsh economic conditions.	0.911
Is your Bank likely to undertake mergers and acquisition to survive the competition and the economic conditions?	0.913
How likely is your bank to undertake M&A in order to obtain synergy from the banks' complementary skills and	0.914
Would your bank decide to go for merger and acquisition in order to improve its brand image or positioning?	0.914
Is it likely that your bank could go for Merger and acquisition decision to increase its capital with less hassle .and meet regulatory requirements?	0.914
How likely is your bank to go for merger and acquisition to enhance its financial performance?	0.913
Would your bank decide to go for M&A in order to strengthen its market position and provide diversified and better services?	0.913
Result	0.915

Sources: Survey data, SPSS output 2025

The result showed that all constructs have excellent reliability with all Cronbach Alpha values exceeding 0.90 threshold. This indicates that the items in each variable are highly correlated and effectively measure the intended constructs. The results give confidence on the reliability of the questionnaire and indicate the validity of analysis from the dataset.

3.7 Data Analysis Method

The primary data collected from the closed ended questions in the questionnaire were analyzed using both descriptive and inferential analysis. In order to do so, Statistical Package for Social Sciences (SPSS) software was employed. The software SPSS was utilized to scrutinize and construe the data through

tabulation, frequency distribution, and statistical analysis. This software was selected due to its robustness and reliability in analyzing social science data, particularly when dealing with survey-based research.

Descriptive statistics are statistical computations describing either the characteristics of a sample or the relationship among variables in a sample. It merely summarizes a set of sample observations, whereas inferential statistics move beyond the description of a specific observation to make inferences about the larger population from which the sample observations were drawn (Babbie, 1998).

In this study, frequencies and percentages were used to describe the demographic characteristics of the respondents based on the frequencies and percentages obtained from the responses regarding the characteristics of respondents.

To address the research objectives and test the hypotheses, inferential statistical methods were employed in this study. Correlation analysis was used to examine the strength and direction of relationships between the identified motives or factors influencing mergers and acquisitions (M&A) and the M&A decision itself. This technique was appropriate as it allowed the study to identify significant associations between variables.

In addition, multiple regression analysis was conducted to evaluate the predictive power of independent variables (motives/factors) on the dependent variable (M&A decision). The reason for applying this analysis method was to quantify the influence of each factor and also to reveal the combined effect of multiple variables, thereby offering deeper insights into which factors most significantly impact M&A decision-making.

3.8 Ethical Considerations

A brief introduction of the central purpose of the study were clearly indicated on the introductory part of the questionnaire to be filled by respondents. The respondents were assured that the responses would be used only for academic purpose and kept confidential. Lastly, the respondents are included in the study voluntarily and based on their own free will.

CHAPTER FOUR

DATA ANALYSIS AND DISCUSSION

I. Introduction

This chapter presents the results of the study. Detailed analysis of the results derived from the questionnaire analysis are presented in this chapter. As stated in the previous chapter, the study used descriptive and explanatory research design.

4.1 Data Analysis

A structured questionnaire was administered to collect the data from 243 top level and middle level managers. Among which, 221 questionnaires were properly filled and collected while the remaining 22 were not filled with a response rate of around 90%. In this section, characteristics of the respondents, the reliability test result and analysis of the independent variables are also presented, analyzed and discussed. The study employed two types of data analysis including descriptive analysis and inferential analysis. First the results of the descriptive statistics reveals the maximum, minimum, mean and standard deviation of variables used in the study. While the inferential analysis part includes the regression result of the multiple regression model that outlines the examination of the relationship between decisions for mergers and acquisitions and various variables in the study was discussed.

4.2 Profile of respondents

The study was conducted on 221 members of top and middle level management at selected private commercial banks. The demographic backgrounds of the sample respondents are presented in five parameters to understand their profiles i.e., gender, age, education, work experience and position.

Table 5: Demographic background of respondents.

Variables	Categories	Frequency	Percentage (%)	Cumulative Frequency
Gender	Male	155	70.1	70.1
	Female	66	29.9	100
	Total	221	100	
Age	20-29	30	13.6	13.6
	30-39	96	43.4	57.0
	40-49	61	27.6	84.6
	>50	34	15.9	100.0
	Total	221	100	
Education Status	BA/BSC	83	37.6	37.5
	MA/MSC	132	59.7	97.3
	PHD	6	2.7	100
	Total	221	100	
Work Experience	1-5 years	12	5.4	5.4
	6-10 years	43	19.5	24.9
	11-15 years	60	27.1	52.0
	16 -20 years	65	29.4	81.5
	>20 years	41	18.6	100
	Total	221	100	
Position	Executive Mgt	27	12.2	12.2
	Middle level Mgt	194	87.8	100.0
	Total	221	100	

Source: Survey result.

Table 4 above depicts the background profile of the respondents. Accordingly, the gender composition showed that 70% percent of respondents are male while 30% percent are female revealing that Ethiopian banks, at managerial level is highly dominated by males.

With respect to the age of respondents, the largest number of respondents fall under the the age range of 30 to 39 which accounts 96 (43.4%), the second highest age is in between 40 to 49 which accounts for 61 (27.6%) whereas respondents above the age of 50 and between the age ranges 20 to 29 took the percentage of

34 (15.9%) and 30 (13.6%), respectively. Therefore, one can conclude Ethiopian banking sector is led by young and energetic individuals.

In the case of the educational qualification of the respondents, 132 (59.7%) of them are Masters Degree holders, 83 (37.6%) are First Degree Holders and the rest 6 (2.7%) are PHD holders. It implies that most of the respondents are well educated.

Concerning work experience, 65 or 29.4% of respondents have experience of 16 to 20 years, 60 or 27.1% of respondents have work experience of 11 to 15 years, 43 or 19.5% of respondents have 6 to 10 years of experience, 41 or 18.6% have more than 20 years of experience while the remaining 12 or 5.4% have 1-5 years experience. These figures have confirmed that majority of the respondents are well experienced.

Regarding the position of the respondents 27 or 12.2% of them are Executive Management members who are responsible for making major decisions concerning the entities operations. The remaining 194 or 87.8% of respondents are senior/middle level managers, who are responsible to implement the plans and strategies developed by top level managers.

The demographic results indicate that most of the respondents are well experienced and educated and are expected to have a good understanding of the issues included in the study.

4.3 Descriptive Statistics on Study Variables

The descriptive statistics were computed for 221 respondents using a 5-point Likert scale (1 = Strongly Disagree to 5 = Strongly Agree). Each item was developed to capture perceptions regarding the drivers of mergers and acquisitions (M&A) in the Ethiopian banking sector. The Likert scale used is a summated rating scale, where an individual's score represents the sum (or average) of responses to multiple items. The results summarized in the table show the minimum, maximum, mean, and standard deviation for each variable, which include seven independent variables and one dependent variable.

Among the drivers assessed, Branding had the highest mean score (Mean = 3.278, SD = 0.859), closely followed by Diversification (Mean = 3.272, SD = 0.892). In contrast, Market Expansion recorded the lowest mean score (Mean = 3.009, SD = 0.912), indicating it is perceived relatively less strongly as a motivating factor for M&A as compared to others.

All variables had mean values ranging between 2.9849 and 3.2776, suggesting that, on average, respondents

tended to respond neutrally to the listed M&A drivers.

Table 6: Descriptive statistics of study variables

Descriptive Statistics of study variables					
	N	Minimum	Maximum	Mean	Std. Deviation
Financial Performance improvement	221	1	5	2.9849	0.90991
Compliance with regulatory requirements	221	1	5	3.0483	0.81382
Market Expansion	221	1	5	3.009	0.9117
Diversification	221	1	5	3.2724	0.89229
Cost saving (Synergy)	221	1	5	3.0109	0.88701
Branding	221	1	5	3.2776	0.85868
Survival	221	1	5	3.1387	0.90471
Merger and acquisition decisions	221	1	5	3.1958	0.7631

Source: Survey data, SPSS output 2025

Based on literature, Likert scale questions are interpreted as per the following ranges, for a given 5-point Likert scale, if the mean lies in the range of 1.00–1.80 = Strongly Disagree, 1.81–2.60 = Disagree, 2.61–3.40 = Neutral, 3.41–4.20 = Agree and 4.21–5.00 = Strongly Agree.

Accordingly, all variables fall within the Neutral range, implying that respondents neither agreed nor disagreed strongly on whether these factors significantly influence M&A decisions in the banking sector. This could be due to cultural aversion to M&A or the dearth of experience in mergers and acquisitions involving share companies in Ethiopia.

N.B. The detailed frequency distribution, mean, and standard deviation for each items are presented in the Appendix.

4.4 Correlation analysis

This section presents a correlation analysis to examine associations between the dependent variable (merger and acquisition decisions) and the seven key independent variables (factors driving M&A). A correlation refers to a quantifiable relationship between two variables, and the statistic that provides an index of that relationship is called a correlation coefficient r , which is a measure of relationship between two interval or ratio variables (Akroush, 2003).

Whether two variables are highly, slightly or no correlation at all depends on the correlation coefficient. The correlation coefficient is always scaled between -1 and +1. If two variables are perfectly positively correlated the correlation coefficient would be +1, if it is perfectly negatively correlated -1 and if there is no correlation at all 0.

According to Cohen (1998), strength of correlations can be interpreted as $r = - + .10$ to $- + .29$ small effect (weak), if $r = - + .30$ to $- + .49$ medium effect (moderate) and $r = - + .50$ to $- + 1.0$ large effect (strong). Significance levels were tested at $p < 0.01$ to determine whether observed correlations are statistically meaningful.

The following table depicts the correlation analysis between variables.

Table 7: Correlation Analysis

	MERA	PER	COMP	MKT	DIV	Cost	BRAND	Sur
MERA	1.0000							
PER	0.8061	1.0000						
	(0.0000)**							
COMP	0.7893	0.6598	1.0000					
	(0.0000)**	0.0000						
MKT	0.7030	0.6196	0.6798	1.0000				
	(0.0000)**	0.0000	0.0000					
DIV	0.6797	0.6580	0.5848	0.5642	1.0000			
	(0.0000)**	0.0000	0.0000	0.0000				
Cost	0.6450	0.5820	0.5202	0.5995	0.8621	1.0000		
	(0.0000)**	0.0000	0.0000	0.0000	0.0000			
BRAND	0.0106	-0.0502	0.0084	0.1169	-0.0450	0.0633	1.0000	
	(0.8759)	0.4578	0.9014	0.0829	0.5054	0.3491		
SUR	-0.0185	-0.0416	-0.0160	0.1091	-0.0351	0.0673	0.8219	1.000
	(0.7847)	0.5385	0.8127	0.1059	0.6040	0.3195	0.0000	
** shows there is statistically significant association between variables at $P < 0.01$								

Source: Survey data, SPSS output 2025

Based on the correlation statistics, the results reveal that financial performance improvement has the strongest positive correlation with M&A decisions ($r=0.806$, $p<0.01$), suggesting that firms are likely to pursue M&A if they anticipate enhanced financial outcome. This is followed by compliance with regulatory requirements ($r =$

0.789, $p < 0.01$) and market expansion ($r = 0.703$, $p < 0.01$), which are also strongly and positively correlated with M&A decisions. These findings underscore the strategic importance of regulatory alignment and market growth in merger decisions. Likewise, diversification ($r = 0.680$) and cost-saving potential ($r = 0.645$) are significantly associated with M&A activity, indicating that they are viewed as driving factors for M&A. However, branding ($r = 0.011$, $p = 0.876$) and survival ($r = -0.019$, $p = 0.785$) have statistically insignificant association with M&A decisions. This implies that the two factors may not be primary drivers in the current Ethiopian banking context.

4.5 Model diagnostic tests

4.5.1 Normality test

A normality test is used to assess when the data has been taken from a normally distributed population which is one of the key assumptions in parametric statistical analysis including Ordinary Least Squares (OLS) regression. Shapiro-Wilk (S-W) is used to test normality by comparing the data to a normal distribution with the same mean and standard deviation of the sample. The normality of residuals was tested using the Shapiro-Wilk test, which is appropriate in this case. The test returned a W-statistic of 0.98835 with a p-value of 0.06949, which is greater than the standard significance level of 0.05. Thus, the null hypothesis of normality was not rejected, suggesting that the residuals are approximately normally distributed. This indicates that the assumption of normality required for OLS regression has been met (Ghasem & Zahediasl, 2012).

Table 8: Shapiro-Wilk normality test

Shapiro-Wilk						
Variable	Obs.	W	V.	Z	Prob>z	
Residuals	221	0.98835	1.896	1.480	0.06949	

Sources: Survey data, SPSS output 2025

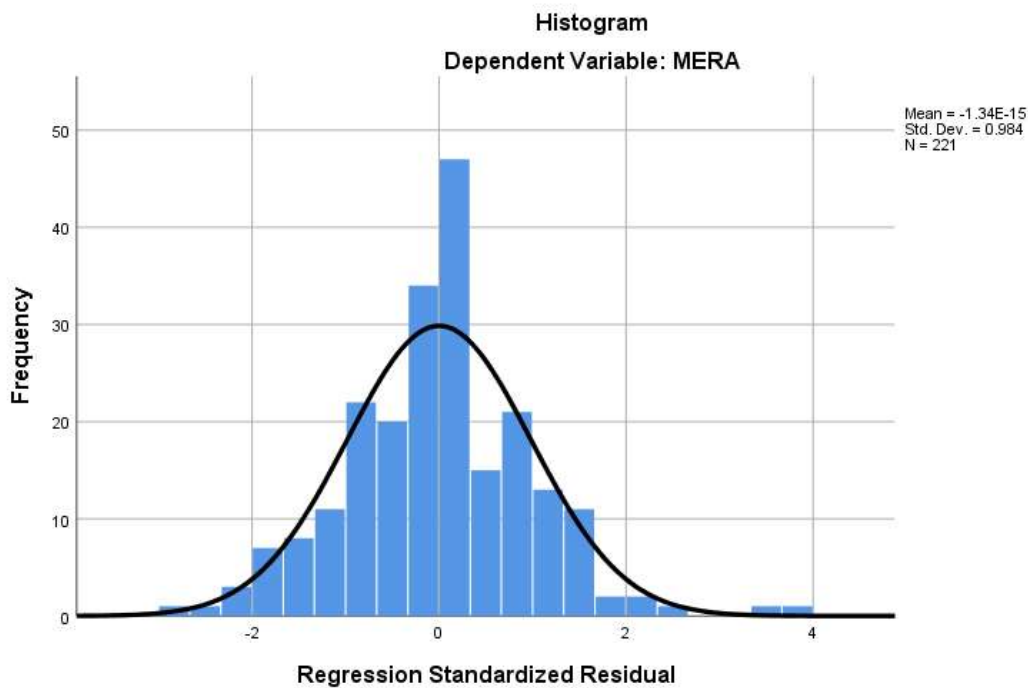
Histogram Test for Normality

In addition to the Shapiro-Wilk test, the study also employed a graphical inspection of the distribution of residuals using a histogram. One of the key characteristics of a normal distribution is that the mean, median, and mode are equal, and the distribution is symmetrical, forming a bell-shaped curve (Ghasem & Zahediasl,

2012).

As shown in the figure below, the histogram of the residuals demonstrates a distribution that approximates normality, with the bars forming a bell-shaped curve centered around the mean. This graphical result supports the result obtained from the Shapiro-Wilk test, further asserting that the assumption of normality for the residuals in the regression model is satisfied.

Figure 2: Histogram Normality test



Sources: Survey data, SPSS output 2025

4.5.2 Test of Heteroskedasticity

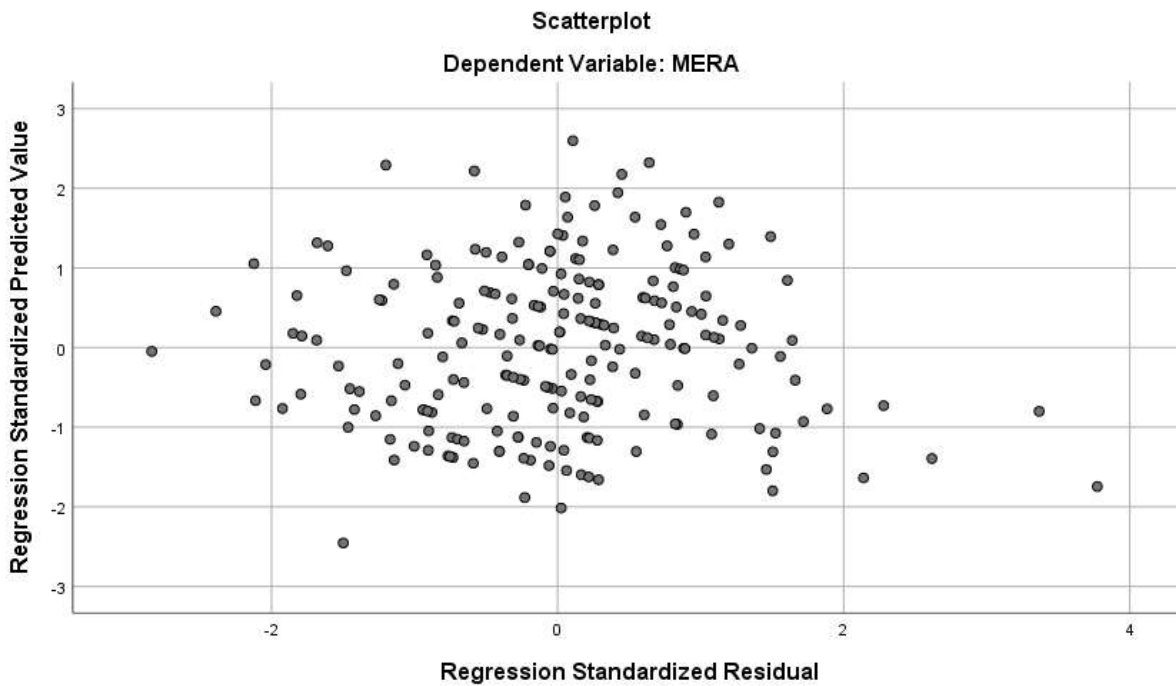
One of the key assumptions in classical linear regression is homoscedasticity, which refers to the condition where the variance of the error terms remains constant across all independent variables. Violation of this assumption which is referred as heteroscedasticity can lead to inefficient estimates and biased standard errors, thus undermining the reliability of hypothesis tests and confidence intervals (Brook, 2014).

To assess the presence of heteroskedasticity in this study, a scatter plot of standardized residuals against predicted values was visually examined. This method provides a graphical check of whether the residuals are randomly dispersed. According to Stevens (2009), if the residuals are scattered randomly around the horizontal axis (zero line) then the assumption of homoscedasticity holds.

As illustrated on the scatterplot below, the residuals appear to be randomly distributed and show no systematic pattern. The dispersion is relatively uniform, suggesting that the error variance remains approximately constant across all levels of predicted values.

Therefore, it can be concluded there is no evidence of heteroscedasticity problem.

Figure 3: Test of Heteroscedasticity using scatter plot



Sources: Survey data, SPSS output 2025

4.5.3 Test of Autocorrelation

Autocorrelation refers to the correlation of the same variables across observations in the residuals of a regression model. To test for autocorrelation, the Durbin-Watson (DW) statistic is employed. The DW statistic ranges from 0 to 4, with a value of approximately 2 indicating no autocorrelation, values approaching 0 indicating positive autocorrelation, and those approaching 4 suggesting negative autocorrelation. Thus, the result given below shows that the Dubin-Watson is 1.835 which is close to 2 suggests that there is no severe autocorrelation among error terms.

Table 9: Test of Autocorrelation

Model Summary ^b					
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin Watson statistics
1	.892 ^a	0.795	0.788	0.35127	1.835
a. Predictors: (Constant), Survival, Compliance with regulatory requirements, Cost saving, financial performance improvement, Market expansion, Branding, Diversification					
b Dependent Variable: Mergers and acquisition decisions					

Sources: Survey data, SPSS output 2025

4.5.4 Multicollinearity test

Multicollinearity problem arises when two or more independent variables in regression model are highly correlated or has a significant relationship with each other. Variance inflation (VIF) is a measure of the degree of multicollinearity in regression analysis. The interpretation is VIF=1, implies that there is no correlation between independent variables, if VIF is in between 1 to 5, and values above 10 indicate there is multicollinearity between predictors in the regression model. Multicollinearity is a concern for multiple regressions not for its existence but its degree.

The following table, shows the mean value of VIF is less than 5 hence, it justifies there is no severe multicollinearity problem among variables.

Table 10: Multicollinearity assumptions and tests

Variable	VIF	Tolerance(1/VIF)
MERA	4.87	0.205147
DIV	4.86	0.205973
Cost	4.47	0.223553
BRAND	3.15	0.317470
PER	3.14	0.318184
SUR	3.13	0.319557
COMP	2.98	0.335701
MKT	2.43	0.410763
Mean VIF	3.63	

Sources: Survey data, SPSS output 2025

4.6 Regression Analysis and model interpretations

Model Fitness tests

To determine the relationship between the independent and dependent variable, multiple linear regressions were used. The coefficient of determination (denoted by R^2) is a key statistic in linear regression that measures the proportion of variance in the dependent variable explained by the independent variables in the model. It ranges from R^2 of 0 to 1 where 0 means that the dependent variable cannot be predicted by the independent variable. The adjusted R square is used to provide a more accurate measure by adjusting for the number of explanatory variables included in the model. If we accurately predict variable then R square (i.e. coefficient of determination) of 0.892 and adjusted R square of .795 is considered good.

In this study the coefficient of determination indicated that the proportion of variance in the dependent variable is explained by the explanatory variables. Based on the result provided below, the coefficient of determination is given an adjusted R-squared of 78.8% it indicated that around 78.8% of the variation in decision for mergers and acquisitions is caused by seven independent variables the remaining 21.2% of the change could be explained by other factors and error term. The output of the model is depicted on the following table.

Table 11: Regression Result of ANOVA

Model Summary ^b				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.892 ^a	0.795	0.788	0.35127
Predictors: (Constant), Survival, Compliance with regulatory requirements, Cost saving, financial performance improvement, Market expansion, Branding, Diversification				
b Dependent Variable: Mergers and acquisition decisions				

Sources: Survey data, SPSS output 2025

To test the overall goodness of fit of the regression model, ANOVA (Analysis of Variance) test was conducted. The ANOVA results presented in the following Table show that the model is statistically significant, with F-statistic of 117.897 and a p-value of 0.000.

Table 12: Regression output ANOVA of the Model

ANOVA ^a						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	101.830	7	14.547	117.897	.000 ^b
	Residual	26.282	213	0.123		
	Total	128.112	220			
<i>a. Dependent Variable: Mergers and acquisitions</i>						
<i>b. Predictors: (Constant), Survival, Compliance with regulatory requirements, Cost saving, financial performance improvement, Market expansion, Branding, Diversification</i>						

Sources: Survey data, SPSS output 2025

The ANOVA table indicated that, the essential information needed to analyze are the degree of freedom, the *f* value and the probability value, overall variance accounted for in the model F- value accounts for (117.897). Moreover, the significance value is less than .05, so it confirms that the regression model provides a better fit to the data. This indicates that, the independent variables reliably predict the dependent variable (mergers and acquisitions decisions).

4.6.1 Discussion and Analysis of regression results

According to Hair et al. (2007), Multiple Regression Analysis, is a form of general linear modeling, is an appropriate statistical technique to examine the relationship between a single dependent variable and several independent variables. The present study is conducted to examine the factors determining mergers and acquisitions in Ethiopia, in the regression analysis decisions for Mergers and acquisitions (MERA) regressed with Financial performance improvement (FPI), Survival (SUR), Compliance with regulatory requirements (CORR), Cost saving (CS), Market expansion (MKTE), Branding (BR) and Diversification (Div). the regression tests employed multiple linear regression. The regression output is provided in the following table.

$$\text{MERA} = 0.451 + 0.340(\text{FPI}) + 0.337(\text{Comp}) + 0.095(\text{Mkte}) + 0.019(\text{Div}) + 0.116(\text{CS}) + 0.057(\text{Brand}) - 0.058(\text{SUR})$$

Table 13: Estimate of Coefficient of Regression Model

Coefficients ^a						
Model	Unstandardized Coefficients			Standardized Coefficients	T	Sig.
		Beta	Std. err	Beta		
1	(Constant)	0.451	0.139		3.242	0.001
	FPI	0.340	0.040	0.405	8.530	0.000
	COMP	0.337	0.045	0.359	7.555	0.000
	MKTE	0.095	0.040	0.114	2.385	0.018
	DIV	0.019	0.058	0.023	0.330	0.741
	CS	0.116	0.056	0.135	2.079	0.039
	BRAND	0.057	0.049	0.064	1.160	0.247
	SUR	-0.058	0.046	-0.069	-1.261	0.209

a. Dependent Variable: MERA

Sources: Survey data, SPSS output 2025

The findings on the individual coefficients shown above revealed that four factors such as Financial performance improvement (FPI), Compliance and Regulatory requirement (COMP), market Expansion (MKTE) and cost saving (CS) had a positive significant impact on Mergers and Acquisitions decisions (MERA) whereas diversification, Branding and survival was not significant determinants of mergers and acquisitions in Ethiopian banks.

Financial Performance improvement and Mergers and acquisitions

The findings indicate that the relationship between financial performance improvement (FPI) and the decision to pursue mergers and acquisitions is statistically significant, with a p-value less than 1% ($P < 0.01$). This means there is strong evidence to suggest that the observed relationship is not due to chance, and we can be at least 99% confident that financial performance plays a real role in influencing M&A decisions.

The standardized beta coefficient ($\beta = 0.340$) further indicates that financial performance improvement has a positive and moderate effect on merger and acquisition decisions. In practical terms, this suggests that as banks place greater emphasis on improving financial performance—such as increasing income or operational

efficiency—they are more likely to consider M&A as a strategic option.

This result aligns with the findings of Hitt et al. (2012), who emphasized that financial performance is often a key driver for firms pursuing acquisitions. Moreover, in the Ethiopian context, as noted by industry experts such as Befekadu (2024), banks often aim to expand capital organically; however, pressures to meet rapid capital adequacy requirements may push some toward M&A strategies.

Compliance requirements and Mergers and acquisitions

The findings show that compliance with regulatory requirements is a statistically significant factor influencing merger and acquisition (M&A) decisions. The p-value is less than 0.1% ($p = 0.000$), indicating a high level of statistical significance. This means there is over 99.9% confidence that the relationship between compliance requirements and M&A decisions is not due to random chance.

The standardized beta coefficient ($\beta = 0.337$) suggests a positive and moderate relationship between compliance requirements and the likelihood of engaging in M&A. This indicates that as pressure to meet regulatory standards increases—particularly capital adequacy requirements—banks are more inclined to consider mergers or acquisitions as a strategic response.

This result highlights the growing role of regulatory frameworks in shaping strategic decisions within the banking sector. One key regulatory requirement is maintaining sufficient capital reserves, which banks must comply with. Non-compliance can result in penalties, fines, or reputational damage, making M&A a viable solution for banks that need to rapidly meet such thresholds.

Based on the above facts, therefore the more compliance requirements smaller banks tend to choose mergers and acquisition rather than facing the challenge as standalone. The finding is consistent with Andersson, (2023), Qaderi, (2017) and inconsistent with the findings of (Baniya & Shah, 2016) who found compliance and regulatory requirements affects MA decisions negatively and insignificantly.

Market Expansion and Mergers and Acquisition

The findings also reveal that market expansion has a statistically significant influence on merger and acquisition (M&A) decisions. The p-value is 1.8% ($p = 0.018$), indicating the relationship is significant at the 5% level. This implies there is a 98.2% level of confidence that the association between market expansion and M&A decisions is not due to random chance.

The standardized beta coefficient ($\beta = 0.114$) shows a positive but relatively weak relationship between market expansion and the likelihood of engaging in M&A. This means that while market expansion is a motivating factor, its influence is less pronounced compared to other variables such as financial performance or regulatory compliance. The positive relationship is reasonable, as M&A is a widely used strategy for entering new geographic or customer markets. By acquiring an established institution, banks can leverage existing customer bases, local market knowledge, and operational infrastructure to quickly scale their presence without building from scratch. This strategy reduces entry barriers and allows the acquiring bank to benefit from the target's reputation and distribution networks. Moreover, existing literatures evidenced that acquiring institutions can increase market share economies of scale by combining operations, processes, redundancies and negotiate with suppliers by increasing purchasing power. As Nguyen et al., (2012) noted that around 80% of M&A have multiple motives of which market timing synergy and response to economic shocks are the most one. Accordingly, in developed countries market forces play a major role while in developing countries monetary authority plays a major role in Bank M&A. In developing countries, Awdeh & EL-Moussawi, (2011) explain market expansion through M&A is common and is often influenced by regulatory frameworks. The result is consistent with Qaderi,(2017) which stated that some companies may be driven to M&A by a goal of gaining market power.

Cost saving/Synergy and M&A

The findings indicate that cost saving or synergy is a statistically significant factor influencing merger and acquisition (M&A) decisions. The p-value is 3.9% ($p = 0.039$), which shows statistical significance at the 5% level, meaning there is 96.1% confidence that the relationship is not due to chance.

The standardized beta coefficient ($\beta = 0.135$) reflects a positive but modest relationship between cost saving/synergy and the likelihood of engaging in M&A. This suggests that while the impact is not as strong as other factors such as financial performance or compliance, cost efficiency still plays a relevant role in shaping M&A decisions.

In the context of the banking sector, cost savings refer to the reduction of operational and administrative expenses, resulting in improved profitability and overall efficiency. Such savings can be realized through streamlining processes, reducing workforce redundancies, merging overlapping operations, and cutting non-essential expenditures. These synergies are often a key rationale for M&A, as they enable banks to operate more efficiently and increase shareholder value. Therefore, the potential for cost savings remains an important strategic driver behind M&A activity.

Darayseh & Alsharari, (2023) investigated domestic bank mergers and acquisitions in Ethiopia as a prudent strategy for efficiency and synergy gain, and they confirm that larger private banks in Ethiopia, are the preferred banks offering efficiency gain from merger and acquisition. It's important to note that cost savings are a key driver of M&As, but the actual cost savings achieved can vary widely depending on the specifics and success of the merger.

Non-significant Factors

Conversely, Diversification, Branding, and Survival did not show statistically significant relationships with M&A decisions. This implies that while these factors may hold theoretical importance, they may not be dominant motivators for Ethiopian banks considering M&A. This may reflect the early stage of market maturity and the absence of diversified product competition in the domestic financial sector.

Summary of Hypothesis Testing

The regression analysis tested seven hypotheses to explore the main drivers of M&A decisions among private banks in Ethiopia. Out of the seven proposed hypotheses, four were accepted based on statistically significant p-values, and three were rejected due to lack of statistical significance. The summary of the hypothesis testing is presented as follows;

Table 14: Summary of hypothesis testing

Hypothesis Code	Hypothesis Statement	Standardized Beta (β)	p-value	Significance Level	Decision
H1	There is a positive relationship between financial performance improvement and merger and acquisitions decision.	0.405	0.000	Significant at 1%	Accepted
H2	There is a positive relationship between compliance with regulatory requirement and merger and acquisitions decision.	0.359	0.000	Significant at 1%	Accepted
H3	There is a positive relationship between market expansion and merger and	0.114	0.018	Significant	Accepted

	acquisitions decision.			at 5%	
H4	There is a positive relationship between diversification and merger and acquisitions decision.	0.023	0.741	Not significant	Rejected
H5	There is a positive relationship between cost saving and merger and acquisitions decision.	0.135	0.039	Significant at 5%	Accepted
H6	There is a positive relationship between branding and merger and acquisitions decision.	0.064	0.247	Not significant	Rejected
H7	There is a positive relationship between survival and merger and acquisitions decision.	-0.069	0.209	Not significant	Rejected

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

This chapter presents summary, conclusions, recommendations and future research directions based findings presented in chapter 4.

5.1 Summary and Conclusions

This chapter presents a summary of the research paper and the results of the study. This research was conducted to assess the driving factors behind merger and acquisition decisions within Ethiopia's private banking sector in light of recent regulatory, policy, and market changes. M&A activity in Ethiopia has historically been minimal, but current structural shifts including the revised minimum capital requirements, the 2024 Banking Business Proclamation allowing foreign participation, and upcoming introduction of Basel II/III compliance, indicate a strong likelihood of consolidation.

As stated in the previous chapter, the study used descriptive and explanatory research design. A structured questionnaire with sample size of 243 was administered to collect data from management members of 16 private commercial banks in Ethiopia. Survey responses from 221 senior bank executives revealed that four key factors i.e. financial performance improvement, regulatory compliance, market expansion, and cost-saving synergies positively and significantly influence M&A decisions. Among these, financial performance improvement had the strongest correlation with M&A decision, followed by compliance and market expansion. On the other hand, branding, diversification, and survival were found to be statistically insignificant drivers in the current Ethiopian banking context.

The regression model proved highly reliable and predictive, with an adjusted R^2 of 0.795, confirming that a significant portion of the variability in M&A decisions can be attributed to the identified independent variables. Model diagnostic tests confirmed data validity, reliability, and the appropriateness of the regression assumptions.

In conclusion, the study validates the role of economic and regulatory forces in shaping bank consolidation in Ethiopia. As banks navigate increasing operational and compliance pressures, M&A emerges as a viable strategy to scale operations, increase competitiveness, and meet evolving regulatory standards.

5.2 Recommendations and future research directions

Based on the findings presented in the previous chapter the following recommendation is forwarded

- 👉 One of the most significant and leading factors in driving mergers and acquisitions is Financial Performance Improvement (FPI). Though the practice of mergers and acquisitions had been scarce in the Ethiopian context, it is now inevitable due to various internal and external pushing factors such as increased capital requirement and liberalization of the sector. Therefore, bank managers, especially private banks, should strategically think and identify the acquiring banks based on historical financial data, have strong agents, have strong asset base and improved technology or digital banking. Otherwise they should consider to be acquired by another stronger bank.
- 👉 One of the critical areas in merger and acquisitions decisions is compliance and regulatory requirements and is the ongoing challenge for both acquiring and acquired institutions. Therefore, bank supervisors being ready for the challenge and consciously understand the legal and regulatory requirements on the ground. The researcher would like extend recommendations for private banks whose fate or trajectory is being merged, should thoroughly understand the various forms of Mergers and acquisitions and their consequences. Moreover, the regulatory body NBE should draft M&A guidelines addressing cultural integration.
- 👉 Another important area of Mergers and acquisitions identified on the regression analysis is market expansion, decision makers should identify banks whose customer base and service potential is significant. Therefore, decision making units (CEO's and BOD) should carefully analyze and understand the market dynamics and the competitive advantages being realized by acquiring specific target banks.
- 👉 M&A in Ethiopia must navigate ethnic ownership, yet this was unaddressed in our model.
- 👉 Finally, the researcher extends future research directions or insights from the findings and discussions. First, besides the above factor future researchers shall extend his/her research by including more variables which trigger for mergers and acquisitions such as asset size, risk, leverages, capital adequacy etc. Second the study would become more conclusive, if it is done separately (by the side of Acquiring and acquired institutions). Third, the issue of mergers and acquisitions as stated by numerous scholars is very complex and time taking, so that more qualitative in-depth analysis is required besides quantitative drivers.

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Annex

Addis Ababa University
College of Business and Economics
School of Commerce Graduate Studies Program
Questionnaire for Employees at Managerial Level

Dear Respondents,

My name is Lidia Samuel. I am a graduate student at Addis Ababa University School of Commerce. This questionnaire is prepared to collect data *from management members of Private Commercial Banks* for my dissertation on the topic of “**Factors contributing to Mergers and Acquisitions in the Ethiopian Banking Industry**” in partial fulfillment of the requirement for *MSC in Corporate Finance with Specialty in Investment Management. Due to the importance of your role in this paper, you have been purposefully selected to participate in this study.* I kindly implore you to respond to the questions as accurately and honestly as possible. It will be of great importance if you complete all the items covered in the questionnaire since your opinion is of utmost importance. Your responses are strictly confidential and will be used only for academic purposes.

Thank you in advance for your time and cooperation!

Lidia Samuel

If you have any inquiries, please feel free to contact me through my E-mail : lidusam@gmail.com

Part I: Profile of Participants

Please answer by putting a tick mark (√) in the box provided.

1. Gender: Male Female
2. Age group: <20 20-29 30-39 40-49 >50
3. Educational Status: Diploma BA/BSC MBA/MA/MSC PHD
4. Number of service years of the participant in the managerial position?
 1-5 6-10 11-15 16-20 >20
5. Current Job Level:
 Executive Management Senior/Middle Management

Part II: M& A Related Issues

Please read each question carefully and select your level of agreement for the following statement. And tick (√) mark the appropriate number from 1 to 5. Each testimonial is measured by 5- point Likert scale: 1= Strongly disagree; 2=Disagree; 3=Neutral; 4= Agree; 5=Strongly agree.

S/N	Factors contributing to M&A in the Ethiopian Banking Sector (Independent variables)	Level of Agreement				
		SDA	DA	N	A	SA
	Financial Performance Improvement					
1	M&A can be pursued for increased revenue by combining customer bases and product offerings.	1	2	3	4	5
2	M&A can help minimize the volatility of earnings of the merging banks.	1	2	3	4	5
3	Merger and acquisition may increase the net interest income (difference in revenue resulting from bank's assets and expenses associated with paying)of banks.	1	2	3	4	5
4	M&As may lead to increased operational and financial efficiency through the consolidation of processes and systems.	1	2	3	4	5

S/N	Compliance with regulatory requirements	SDA	DA	N	A	SA
5	M&A may occur if banks are not able to meet the paid-up capital increase requirement set by the National Bank of Ethiopia (NBE).	1	2	3	4	5
6	M&A could take place among banks having trouble with meeting the deadline set to meet the capital requirement criteria.	1	2	3	4	5
7	M&A may occur between local banks as foreign banks are now allowed to operate in the country.	1	2	3	4	5
8	Banks may be forced to merge by the regulator (statutory merger) to bring efficiency and effectiveness among the banks.	1	2	3	4	5
9	Change in banking regulation standard, i.e. a shift from the current Basel I standard to advanced ones, can lead to M&A of banks.	1	2	3	4	5

	Market Expansion	SDA	DA	N	A	SA
10	In order to obtain power to exclude rivals, banks go through merger and acquisition.	1	2	3	4	5
11	Merger and acquisition have roles to capture better market share.	1	2	3	4	5
12	Merger and acquisition are used to increase market power when the bank acquires another bank in different geographical area.	1	2	3	4	5

13	Merger and acquisition is an effective tool to execute expansion strategy of banks.	1	2	3	4	5
14	Merger and acquisition can provide banks with access to new markets and customer segments, leading to increased competitiveness.	1	2	3	4	5

	Diversification	SDA	DA	N	A	SA
15	In order to diversify and offer wider range of products/services to the customers, merger and acquisition is done.	1	2	3	4	5
16	M&A is done to provide diversification of funding sources, as the merged entity can have access to a wider range of funding options and capital sources.	1	2	3	4	5
17	In order to achieve geographic diversification, merger is done with banks having deeper market penetration and broader reach.	1	2	3	4	5
18	M&A is done to provide diversification of the loan portfolio, as the merged entity can benefit from a more diverse range of loan products and customer segments.	1	2	3	4	5
19	As part of related diversification, M&A can be performed to minimize and diversify risk in the market.	1	2	3	4	5

	Cost Saving (synergy)	SDA	DA	N	A	SA
20	Merger and acquisition can help to minimize the duplication of banking activities, processes and systems through consolidation of operations.	1	2	3	4	5
21	In order to achieve economies of scale M&A can be done, as the merged entity can benefit from lower costs associated with larger scale operations.	1	2	3	4	5
22	M&A will provide access to better technology, which can improve operational efficiency and reduce costs.	1	2	3	4	5
23	M&A can be done to create synergies from shared services, as the merged entity can benefit from the consolidation of functions such as finance, Marketing, HR, Services and IT.	1	2	3	4	5
24	In order to produce more without increasing the individual capacity of banks, merger and acquisition is performed.	1	2	3	4	5

	Branding	SDA	DA	N	A	SA
25	Merger and acquisition is done to increase the positioning of banks in the mind of the customers.	1	2	3	4	5

26	Merger and acquisition makes it possible to improve image of banks with less activities to be performed than had they done individually.	1	2	3	4	5
27	Merger and acquisition helps to obtain better branding of banks within short span of time.	1	2	3	4	5
28	Merger and acquisition helps to create the brand of banks with involvement of less cost than had it been done individually.	1	2	3	4	5
29	Merger and acquisition makes it easy for the advertisement of banks to reach to large number of consumers than had it been done alone.	1	2	3	4	5

	Survival	SDA	DA	N	A	SA
30	M&A can be pursued as a survival strategy to mitigate financial distress and reduce the probability of bank failure.	1	2	3	4	5
31	M&A can be done to withstand the competition and gain competitive advantage in the market.	1	2	3	4	5
32	New entrants to the sector may pose existential threat for the existing smaller banks and hence lead them to M&A decision.	1	2	3	4	5
33	Merger and acquisition will make banks secure from various environmental factors such as economic, political, socio-cultural as well as technological factors.	1	2	3	4	5
34	M&A can help banks to survive during harsh economic conditions.	1	2	3	4	5

Part III: M&A Decisions Related Questions

	Merger and acquisition decision (Dependent variable)	SDA	DA	N	A	SA
35	Is your Bank likely to undertake mergers and acquisition to survive the competition and the economic conditions?	1	2	3	4	5
36	How likely is your bank to undertake M&A in order to obtain synergy from the banks' complementary skills and weaknesses and reduce costs?	1	2	3	4	5
37	Would your bank decide to go for merger and acquisition in order to improve its brand image or positioning?	1	2	3	4	5
38	Is it likely that your bank could go for Merger and acquisition decision to increase its capital with less hassle and meet regulatory requirements?	1	2	3	4	5
39	How likely is your bank to go for merger and acquisition to enhance its financial performance?	1	2	3	4	5
40	Would your bank decide to go for M&A in order to strengthen its market position and provide diversified	1	2	3	4	5

	and better services?					
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41. What additional factors do you think will influence your bank's or the private banking sector's M&A decisions in general?

(Source: Questionnaire adopted from (Baniya and Shah, 2016) and (Terefe, 2022))

Thank you!!!