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FACTORS NECESITATING MERGERS AND ACQUISITIONS: THE CASE OF PRIVATE COMMERCIAL BANKS OF ETHIOPIA

A Thesis submitted to Addis Ababa University, College of Business and Economics, in Partial Fulfillment of The Requirements for the Degree of Master of Business Administration (MBA).

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Addis Ababa, Ethiopia

DECLARATION

I, Assefa Terefe, declare that this thesis work entitled “*Factors Necessitating Merger and Acquisition: The case of Private Commercial Banks in Ethiopia*” is my original work undertaken for partial fulfillment of the requirement for the Degree of Master of Business Administration at College of Business and Economics, Addis Ababa University. The thesis in full or in part has not been submitted for any purpose academic or otherwise anywhere.

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LIST OF ABBREVIATIONS:

ADLI = Agricultural development led industrialization

CBE = Commercial Bank of Ethiopia

CEO = Chief executive officer

EC = Emphasis on Cost

EFD = Emphasis on Financial Diversification

EI = Emphasis on Income

EMC = Emphasis on Market Expansion

EME = Emphasis on Market Expansion

EPS = Earnings per share

ETB = Ethiopian Birr

EU = European Union

FDI = Foreign direct investment

GDP = Gross domestic product

M&A = Mergers and acquisitions

MFI = Micro finance institution

NBE = National Bank of Ethiopia

ROA = Return on asset

ROCE = Return on capital employed

SPSS = Statistical Package for Social Sciences

UN = United Nations

US = United States

USD = United States Dollar

WACC= Weighted average cost of capital

ABSTRACT

Despite recent developments every sector of the economy, Ethiopia remains naïve to the practice of M&A. There are no well documented M&A activities, if any. Previously, sufficient research is not conducted by scholars on M&A activities and factors that affect merger and acquisition on private commercial banks in Ethiopia. The objective of this study was to find out what factors do objectively trigger merger and acquisition of the private commercial banks of Ethiopia. The study is quantitative and primary data was collected using structured questionnaire. Explanatory research design was employed to conduct this study. Convenience (non-probability) sampling technique is used to select participants of the study. The result was analyzed and interpreted by applying inferential statistics. Since the questionnaire is Likert scale type the best way to analyze the data is linear regression. Multiple linear regression model is employed in this study. It was found that among the factors expected to necessitate merger and acquisition, the regression result showed that emphasis on operational cost reduction and increasing income necessitate mergers and acquisition. The factors emphasis on market expansion and emphasis on maintaining capital requirement are also found to necessitate merger and acquisition. The hypothesis emphasis on product diversification was not significant motivator of merger and acquisition. Banks which do not want either to merge or to be acquired, therefor need to increase their income, decrease operational costs, capture adequate share of the market and should raise their capital requirement set by the NBE.

Key words: Mergers, acquisition, financial system, motives, globalization.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Globalization has led to the emergence of new business ventures. Mergers and acquisition of firms seem to be the best approach to tackle competition. The terms merger and acquisition are often used interchangeably even if they have distinct denotations (Pol, 2020; Soundarya et al., 2019). Many companies view acquisitions and alliances as interchangeable strategies for spurring growth. But each strategy has unique advantages and disadvantages (Dyer et al., 2004). The difference between merger and acquisition lies in the way in which the combination of the two companies is brought about. Merger or Acquisition in a Company Sense Can be defined as the Combination of two or more Companies in to one new company or Corporation.

Before merger of two companies is brought there is a process of negotiation between the parent companies. A Merger is a combination of two corporations in which only one corporation survives. The merged corporations typical ceases to exist. The acquirer gets the assets of the target but it must also assume its liabilities. Sometimes there is a combination of two companies that are of similar size and where both of the companies cease to exist followings the deal and an entirely new company is created. In a merger the smaller company is considered as the target company and the larger company is considered as the buyer company. M & A are not different. When one company acquires another in a hostile situation it is referred to as takeover. This happens when one company tries to acquire another against the will of the target company management and board (Gaughan, 2005; Roberts & Wallace, 2016).

In an acquisition one company, the target, is directly owned by another company, the acquirer. The acquired company may totally be absorbed and cease to exist as a separate entity or may exist as pre-acquired state based on the will of the acquired company. In an acquisition the dominant company is referred as the acquirer and the acquired company is called as the target Company. In an acquisition the acquirer acquires the target by buying its share up to the point where it becomes the owner. Acquisition can be friendly or hostile (Roberts & Wallace, 2016). An Acquisition Activities by which acquiring firms can control more than 50 % of the equity of target firms whereas in a Merges at least two firms are combined with each other to form a 'new' Legal entity. A Merger is a combination of two or more businesses in which only one of the corporations survives (Piesse et al., 2013).

Merges can be defined from legal and economic perspectives. In a legal perspective, a merger is a combination of two or more firms often comparable size, in which all but none ceases to exist. Legally statutory or direct merger is one in which the acquiring company assumes automatically the assets and liabilities of the target in accordance with statutes of the state. A subsidiary merger involves the target becoming a subsidiary of the parent. A statutory consolidation which involves two or more companies joining to form a new company, technically is not a merger. All legal entities that are consolidated are dissolved during the formation of the new company and has a new name. From economic perspective, business combination can be defined depending on whether the merging firms are in the same (horizontal) or different industries (conglomerate) and on their position in the corporate value chain (vertical) (DePamphilis, 2017).

In an acquisition, the acquirer, the dominant company purchases majority of the shares of the other company, the target. In a merger a new company is formed in which the merging companies share broadly equal ownership. The motives of M&A, acquirer types and dynamics is different.

The aim of M&A transaction is to generate new or better value in some form. Since the end of 19th century M&A has played a great role in advancing firms' competitive advantage, renewal, and growth most M&A deals have failed to achieve the envisioned economic and strategic goals. M&A is described as one company, acquirer, purchasing majority of the shares over 50% of another company, the target (Junni & Teerikangas, 2018).

Merger is the aggregation of two or more firms which results in continuous function of one firm. It is a unification of two business where one exists and the other moves out of business. It is a voluntary fusion of companies. An acquisition occurs when one company takes a controlling ownership interest in another firm a legal subsidiary of another firm. In other words, an acquisition is the purchase of an asset such as a plant, a division or even an entire company. The decision may be friendly or hostile (Soundarya et al., 2019). Merger and acquisition take place when two or more companies are brought under the same effective control and are managed by the same group. Acquisition is the acquiring of one business by the other. Whereas merger is the creation of new company by complete consolidation of two or more units (Rohra & Chawla, 2015).

M&A is very risky and many deals fail, brings companies to the brink of failure. The reason of failure ranges from opportunistic M&A, overpayment to poor integration. According to different academic literatures failure rates ranges from 50-80%. Factors that raise the probability of success in M&A include; strategically motivated deals, acquisition of related business, acquisition of private firms, large related deal, buyer obtained control, buying during cold M&A markets, cost and capex related synergy, frequent acquirers and negotiated deal. M&A have increasingly become an important part of the corporate strategy of many companies (Pol, 2020).

In reality management team acquire or merge businesses without having thought the market dynamics. The major cause of M&A failure is people related while other problems stem from lack of structured approach. Sometimes managers may overestimate their own ability to manage acquisitions; myopically focused on earnings per share and make errors which leads to failure of the M&A. Physical and financial resources alone cannot improve efficiency of an organization by themselves. Human resources are one of the most vital resources for successful merger and acquisition (Chandrashekar Krishnamurti, 2008; Soundarya et al., 2019).

The field of merger and acquisition has typically expanded over the past quarters of a century. M&A seems to be a U.S business phenomena, however, it turned to expand to the world in the 1990. European countries in the 2000, and Asian countries like Japan and Korea saw restructuring of corporation (corporate restructuring) witnessed a great level & M&A (Gaughan, 2005). M & A are not confined to the banking industry. They take place in other industries like media and entertainment sector, automobile industry and the telecommunication sector. Until 1980s the financial industries in the EU member states operate in a highly regulated markets and government ownership played a more significant role. M & A are changing the structure of the EU banking sector. The change in the structure of the EU banking sector was, however, due to driving forces like information technology, disintermediation and the integration of international capital market and creation of single currency, the Euro. The M & A activity in Europe shows different patterns depending on the market sector (mutual banks, publicly owned banks, saving banks) and size of the market, thus size of the institution by international comparison. M&A can lead to the establishment of financial conglomerates, which is active in different sectors of the financial industry. The largest company in a conglomerate may be created by credit institution, insurance companies, holding company or another financial institution.

Financial conglomerates may be created by a M&A or by a financial institution setting up a company in another sector. For example, a bank setting up an insurance company to expand into the insurance sector. Financial conglomerates can be domestic or international, containing financial institutions of different countries (European Central Bank 2000).

M&A, the stuff of newspaper headlines, quite often fail. According to several studies conducted over the past four decades around 50% of mergers don't achieve their business objectives. Despite this fact, companies from developing countries such as China, India, Malaysia, Russia, and South Africa are using M&A as their main globalization strategy today. Unlike Western companies, which use M&A primarily to increase size and efficiency, emerging giants acquire firms to obtain competencies, technology, and knowledge essential to their strategy. When emerging giants pursue cross-border acquisitions in particular they don't search for traditional synergies or to try to lower their costs. They buy western companies to gain complementary competencies, i.e to learn how to deploy assets such as technologies and brands and innovation skills which will help them become global leaders. Emerging giants, companies from highly developing countries, use novel integration techniques and measure performance in light of long-term goals. Western companies have clear short-term aims but may not have thought through long-term goals while emerging giants have fuzzy short-term goals but clear long-term vision when looking for M&A. Being a low-cost commodity player, emerging giants look for a value-added branded-products company to achieve synergy. In Western companies, however, the merging and acquiring companies have the same business model and the same market approach (Nirmalya, 2009).

1.2 Background of Ethiopian Economy

Ethiopia had a command economic policy in the period 1974-1991 with little space for private sector. In 1991, after the fall of the Dergue regime, Ethiopia introduced market-oriented economy with strong role play by the state. The policy was known as Agricultural development led industrialization (ADLI). The police aimed to achieve successful industrialization through agricultural development and its linkage with other sectors of the economy. It implemented an extensive investment in the agricultural sector. During the past three decades the share of the agricultural sector in the Ethiopian economy has decline from 63% of GDP in 1992 to 33% in 2019. The sharp decline of the share of agriculture in the GDP is accounted a 10% and 20% increase in the service and industrial sector respectively. The vast majority of Ethiopia's GDP is composed of the service and agricultural sector (Garrow & Holbeche, 2000).

In 2020/21 fiscal year the GDP of Ethiopia at current market price was 4.3 trillion ETB. The nominal GDP growth rate and average exchange rate were 28.6% and 38birr/USD respectively. The total population of Ethiopia is stated to be 101.9 million according to the report made by the NBE. The real GDP growth rate is 6.3%. The general inflation in 2020/21 was 20.2% which is higher to that of the 2003/04, 7.3% (National Bank Ethiopia, 2021).

The manufacturing of goods in the merchandise export has been declined. The low and declining share of manufacturing export in Ethiopia indicates that the economic growth over the past two decades has not resulted in the desired structural transformation. This is because the exporting manufacturing goods needs sophisticated technology and involves more complex global chains. The country's economic complexity index (ECI) rank was increasing in 2005 but latter decreased to a level below where it has been in 1995. The average GDP growth rate was 9.6% with a

standard deviation of 3.3% since 2004-2019. The growth of GDP was due to large public investments mainly financed by foreign borrowing (Garrow & Holbeche, 2000).

The average trade deficit between 1991 to 2003 was 10% and increased to 17% in the period 2003-2020. FDI was almost non-existent in the early 2000s. Since 2003/04, it turned up to be a source of financing for the country, reaching 31% of the trade deficit. Yet it showed signs of decline since 2016. The budget deficit was financed by external and domestic borrowing. Before 2003/04 period 63% of the budget deficit was financed by external borrowing and 33% were covered by domestic borrowing. After 2003/04 the role of domestic borrowing in financing budget deficit raised to 52% and during the last five years it has reached to cover 63% of the total budget deficit. The CBE accounts for 57% of domestic mobilization as of 2019/20. The average inflation rate since 2003/04 was 15.13% (Garrow & Holbeche, 2000).

1.3 The Financial System of Ethiopia

The beginning of modern banking business starts in Ethiopia after the establishment of Abyssinian Bank in 1905. It was dominated by foreign ownership, until it was bought by the government of Ethiopia in 1931 and renamed Bank of Ethiopia. There by Abyssinia Bank became the first African bank to be nationally owned. Despite considerable British opposition, state bank of Ethiopia was established in Ethiopia. Resistance to foreign control of the financial sector is a long-standing theme until today. Bank of Ethiopia operated as both Central and commercial bank as of 1963. But after 1963, it was dissolved to form the Central bank, called the National Bank of Ethiopia and the commercial bank, named Commercial Bank of Ethiopia. The NBE started its job since January 1964. Ethiopia had securities market in the 1960s and 70s. The market was closed because of change of policy by the Dergue in 1974. Currently Ethiopia has no securities market (Garrow & Holbeche, 2000;T. Adison, 2001).

During the era of state socialism, 1974-1991, the role of Ethiopia's financial institutions were executing the national economic plan, financing state enterprise state according to government priority plan. Since 1991, the role of NBE is re-formulated, new financial institutions emerged and the role of private sector in the financial sector expanded. (Garrow & Holbeche, 2000).

The financial sector currently operating in Ethiopia is composed of formal, semi-formal and informal institutions. The formal financial system which consists of banks, insurance companies and microfinance institutions (MFI) is a regulated sector. The saving and credit cooperatives are considered as semiformal financial institutions as they are not regulated and supervised by the NBE. The informal financial institutions in the country consists of unregistered traditional institutions such as Iqub (Rotating savings and credit association), Idir (Death benefit association) and money lenders. As of 2020/21 the financial sector of Ethiopia is composed of three government banks, eighteen commercial banks and thirtynine MFIs (National Bank Ethiopia, 2021; Shiferaw, 2019).

The insurance company is under developed, uncompetitive and there exists paucity of information on the kind of life insurance that is currently present. The insurance sector is dependent on the banking sector for much of its new business. Microfinance institutions (MFI) provide financial services, mainly credit and savings. They use joint liability, social pressure and compulsory saving as an alternative to the conventional collateral (Shiferaw, 2019). The NBE Ethiopia is granted the power to promote development of traditional savings institutions of the society along with the microfinance institution and to encourage participation of banks and other financial institutions in the provision of microfinance by a law enacted in July 1996 (Abay Ymer, 2011). Banks are free to charge any interest rate on the loans they extend. The government introduced the rule that commercial banks allocate 27% of their loan portfolio to purchase NBE

bond which then will be transformed to development bank of Ethiopia (DBE) to finance investments which have long term development impact in the country. (Telaye, 2021).

According to World Bank African Development indicators the Central Bank intervention rate is 425%. In order to automate supervision function and submission of regulatory information from banks and MFIs, the NBE has implemented a system called Bank Supervision Application (BSA). BSA is a web-based solution responsible for securing submission of financial information, validation and analysis and report generation (Melese Asfaw, 2014; Shiferaw, 2019).

The impact of world economic distress and globalization is almost negligible as banking sector is not well liberalized (Melese Asfaw, 2014). The principal objective of the monetary policy of the NBE is to maintain price and exchange rate stability and support sustainable economic growth of Ethiopia. Price stability is a proxy for macroeconomic stability which is vital in private sector economic decision on investment, consumption, international trade and saving. (National Bank Ethiopia, 2009).

1.4 Statement of the problem

Despite recent developments in every sector of the economy, Ethiopia remains naïve to the practice of M&A. There is no well-developed regulation that governs merger and acquisition, if any. Ample research is not conducted by scholars on M&A activities, pre and post-merger performances of firms.

The banking sector is highly growing following the change of regime in 1991 GC. After 1991 the national economy was declared to be free market, following this the banking sector was deregulated. Following the deregulation many private banks emerged. Currently Ethiopia has

seventeen functioning private bank and many more are on the process of establishment. The NBE has issued a new regulation in 2021. As per the new directive the NBE set the minimum paid-up capital required to start banking business to 5 billion ETB. Prior to the new directive the minimum paid-up capital to start banking business were 500 million ETB. The new directive installs the minimum paid-up capital requirement not only to banks on the process of establishment and to be established but also to previously established and functioning banks. Established and operational banks are required to raise their minimum paid-up capital to the new minimum, 5 billion ETB, within five years from the declaration of the new directive by June 30, 2026. (National Bank Ethiopia, 2021) Four banks have already surpassed the requirements from the central bank to meet the minimum paid up capital requirement. Four other banks are getting closer to it. It is highly expected that the new directive will trigger a wave of M&A transaction in the history of the banking sector (Meshesha, 2000; National Bank Ethiopia, 2021).

Undercapitalized private banks then remain with potentially two options in the future. Either they have to issue new shares to the public and fulfill the new minimum paid-up capital requirement or undergo M&A with other private banks.

Mergers and acquisition seem inevitable among private commercial banks in Ethiopia. As merger and acquisition is looming in Ethiopia the factors that trigger M&A need to be investigated. The factors which significantly lead to M&A are different from country to country. Those factors which trigger M&A in private commercial banks of Ethiopia are not studied so far. Factors discussed in the literature haven't been analyzed whether they are significant determinants of M&A of private commercial banks in Ethiopia. Merger and acquisition pattern and its determinants are not well studied in Ethiopia.

1.5 Objective of the study

1.5.1 General objective:

The general objective of this study to find out what theoretical motivators of M&A in the literature are significantly important to cause M&A of private commercial banks in Ethiopia.

1.5.2 Specific objectives:

to investigate whether higher capital requirement by regulatory body triggers M&A of private commercial banks.

to study the desire to expand market share of banks can motivate M&A of commercial banks

to investigate whether the need to minimize operational cost triggers M&A of commercial banks

to identify whether the demand of banks to increase income triggers M&A of commercial banks

to study whether product diversification leads to M&A activity

1.6 Significance of the Study

Research on mergers and acquisition have been exhaustively carried out in developed countries. In fact, they have a well- developed and liberalized financial system. But in developing countries like Ethiopia not only research on M&A is lacking but also the real practice of M&A activities is very poor. The increasing number of banks has forced the government of Ethiopia to tighten the capital requirement needed to establish banking business. The declaration of high capital requirement will make banks to invest in equity sale or merger with competent banks. This study will be a pioneer in its type to present what factors really matter to trigger M&A of commercial banks in Ethiopia. It will serve as source of information for further study in the same topic.

1.7 Scope of the Study

The study focuses on the factors that could affect the merger and acquisition activities of private commercial banks in Ethiopia. It will not include public banks as there is no free system of merger and acquisition process between public owned banks and private commercial banks. This study will investigate the potential factors which trigger M&A activities of private banks. It will strive to test which theoretical factors mentioned in the literature do affect the M&A of private commercial banks in Ethiopia.

1.8 Limitation of the Study

This study is a pioneer for further study on mergers and acquisitions. There has not been well documented merger and acquisition activities not only in Ethiopia but also in other African countries. Nonexistent of literature on domestic mergers and acquisition processes and activities is a factor that poses a limitation. The study focuses on private commercial banks and the result will not implicate the factors that motivate M&A activities between public banks and private commercial banks.

1.9 Organization of the Study

The organization of the paper starts by providing an introduction about merger and acquisition activities. Chapter one provides the background of the study, the macro economy of Ethiopia, the financial system and history of banking in Ethiopia. Variables, statement of the problem, significance of the study, scope and limitation of the study are described in chapter one.

Chapter two presents the literature review part of the study. In this chapter theoretical and empirical factors that contribute to the initiation of mergers and acquisition are described. Conclusion about the factors that motivate M&A activities and research gap are also presented.

Chapter three contains the methodology of the study. This chapter has a detailed description of research design, research approach type and source of data. It also presents the population of the study, sampling frame and method of sampling, method of data collection as well as the data analysis method.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

Participation of private and foreign sector is very much necessary for the development of banking sector especially to the developing countries. Involvement of private and foreign sector leads to competition which ultimately brings quality of services and products to customers. The globalization of international markets and the widening of cross boarder activities have made businesses ever more global. The implementation of financial liberalization and deregulation of banking sector led to the proliferation of M&A all over the world, domestic or across boarder (Awdeh & EL-Moussawi, 2011; Baniya & Shah, 2016). Globalization demands importance of expanding into new market not only to compete but also to gain new opportunities (Sarika & Vasantha, 2018). The radical changes in the function and structure of financial markets and the regulation reforms have made the services provided by the financial institution became reasonably different. The last decade in the financial sector has witnessed increasing convergence of banks and insurance companies. Now a day's banks offer insurance while insurance company products compete with bank savings. The potential triggers of M&As can be market deregulation and liberalization, customer's desire for large service providers, increase in stock prices and low interest rates. A rising equity markets and low interest rates generate favorable environment for M&As. New forces of changes that lead to M&A are globalization, structural deregulation, prudential reregulation and technology developments. In recent decades, globalization, deregulation and liberalization has potentially affected all industries (Pinter, 2011).

2.2 Review of Theoretical Literature

A motive is a reason for doing something. It is concerned with the strength and discretion of behavior and the factors that influence people to behave in certain ways. Motivation has three components (Arnold, 1991). These are discretion; what a person is trying to do, effort; how hard a person is trying to do, Persistence; how a person keeps on trying. Motivation could be intrinsic or extrinsic. Intrinsic motivation arises from the self-generated factors that influence people's behavior. It arises when individual feels that their work is important, interesting and challenging and provides them with a reasonable degree of autonomy, opportunities to achieve, and advance and scope to use and develop their skills and abilities. Intrinsic motivation is based on the need to be competent and self-determining. High performance is achieved by well-motivated people who are prepared to exercise discretionary effort.

Extrinsic motivation occurs when things are done to or for people to motivate them. These include reward and punishment. Extrinsic motivators have immediate and powerful effect but do not last long, while intrinsic motivators have deeper and long-term effect as they are inherent to individuals or groups (Armstrong M, 2014).

There are many reasons why acquirers choose to acquire. From an economic efficiency perspective, bidders initiate mergers to create value. Good managers may acquire poorly performing firms and create value by firing target company's management and improving target company operating performance. Financial synergy may be a factor to create value. If the market is inefficient and undervalues the target, the bidders who correctly valued the target can buy the target cheaply and create value (Chandrashekar Krishnamurti, 2008). Most acquisitions come about either because the acquirer's management has spotted an opportunity for growth or because they have identified an issue which is restricting their growth (Creighton, 2013).

The current M&A cycle is driven by the search for growth in the post crisis low growth world, exceptionally low interest rates and abundant liquidity. M&A is facilitated by exceptionally low costs of financing and abundant liquidity, which are the results of unorthodox measures central banks have taken to revive economic growth. In the M&A market corporate acquirers are competing against private equity firms and sovereign wealth funds. M&A is an important strategic option that companies can leverage to make necessary leaps in the competitive market place. It helps companies to obtain a higher market share and broader customer and gain access to new technology, products and distribution channels. M&A is increasing in most sectors like manufacturing and financial services. The typical drivers of M&A include market share, government policy, regulation, limitations, buying out competitors, business synergy, market access and acquiring specific competence (Garrow & Holbeche, 2000; Pol, 2020).

There are different motives for companies to enter M&A. These are shareholder gains, managerial gains, economics of scale, economics of scope, cost saving, tax exemption, diversification, to raise entry barriers, to obtain multimarket contact and to have better research and development (Dyer et al., 2004). Mergers between competitors offer the greatest potential shareholders value creation at the same time they face greatest scrutiny. The motives of financial consolidation can generally be classified into two broad categories.

1 Synergy (Economic motives)

2 Agency or managerial motives

Synergy refers to all motives that serve as value maximization whereas agency related motives include non-value maximization factors (Thanou & Daskalakis, 2013).

Motives why M&A happen can be categorized as:

1. Synergy: Synergy is the value realized from the incremental cash flows generated by combining two businesses. If company A has value of \$a and company B has value \$b then the value of the merged company between A&B is greater than the sum of the values of each separate company. Value of (merged A&B) > value A + value B. Synergy can be operation or financial. Synergies are benefits that can only come about when two entities are joined together: “two plus two equals five”. To enhance shareholder value, the value of two business entities joined together must be greater than when they were separate. Synergy refers the concept that the new formed entity is combination, through the fusion of their skills and capabilities (Awdeh & EL-Moussawi, 2011; Gaughan, 2005).

Value (A+T) > Value A + Value T where, A = Acquirer T = Target (Creighton, 2013).

It is the capability to make a corporate combination more profitable than that of the two individual firms. Synergy also means an increase in competitiveness and resulting in cash flows beyond what the two companies are expected to accomplish independently. The means that lead to synergy are replacing inefficient management, economies of scale and more efficient marketing. Operational synergy can be achieved through vertical or horizontal mergers (Larsson & Wallenberg, 2002).

1.1 Operating synergy: Operating synergy is the real value gains from the combining of two or more individual companies. The main source of operating synergy is the relative cost reduction with the increased production, which are results of economies of scale and scope (Awdeh & EL-Moussawi, 2011).

Economics of scale: refers to the reduction in average total cost for firm producing a single product for a given scale of plant due to the decline in average fixed costs for large production

volume and wide market access. Scale is fixed costs that do not alter in their cost in the short run. Economies of scale also affect variable costs by reducing purchased material prices due to an increase in bulk purchase. Economics of scope: refers to the reduction in average total costs due to a decline average fixed and variable costs when separate firms merge to form a single firm. Having a single department like accounting and firm to support multiple product line and sales force selling multiple products rather than single product. Achieving economies of scale has been suggested to be the main objective of horizontal mergers (DePamphilis, 2017; Thanou & Daskalakis, 2013).

Economies of scope are the main rational for 'small' bank M&A. Small institutions aim to achieve critical mass to explore synergies arising from size and diversification. Economies of scope refers to the capacity of a company to make use of one set of input to offer a large collection of products and services (Larsson & Wallenberg, 2002). Economies of scope can be cost based or revenue based. Cost based economies of scope can be achieved by offering a broad range of products or services to a larger customer base and originate from fixed costs incurred in gathering an information from database or customer equipment. Revenue based economies of scope emerge from the firm's ability to utilize one set of inputs to offer a broader range of products and services through cross selling to an existing customer base. Scope economies: represent the ability of reducing the average per unit cost by producing more than one product concurrently. It can be realized through joint production and marketing. Economies of scope exists when the cost of production of goods A and B jointly is less than the production costs separately (Awdeh & EL-Moussawi, 2011; Thanou & Daskalakis, 2013).

Complementary technical assets and skills: skills and knowledge possessed by one company can be used by the other company to fill gaps created by shortage of similar knowledge and skills. A

company having research and development department can help have advantages when merging with company that do not have such department.

1.2. Financial synergy: Financial synergy refers to the reduction in the acquirer's cost of capital due to a merger or acquisition. Financial synergy occurs when the merged companies have cash flows arising from uncorrelated products. Corporations moving to different product lines whose cash flows are uncorrelated reduce only firm specific risks i.e. systematic risk. Such firms are better able to withstand the loss of customers, suppliers, employees or impact of financial distress than single product firms (Chandrashekar Krishnamurti, 2008; DePamphilis, 2017).

Synergies are benefits that can only be achieved by putting two businesses together. They can be classified as

Commercial synergies: Benefits that come from improvements in the underlying business companies. These include increased sales volume, ability to charge higher prices, reduced production or administration costs and greater efficiencies.

Financial synergies: are the benefits that come from better use of capital. They are reduced cost of borrowings or the cost of equity capital, reduced company tax charge, use of surplus cash and improving the mix of equity and borrowings. Financial synergies are usually reflected in lower weighted average cost of capital (WACC) and improved earnings per share (EPS).

Asset synergies: are the benefits that come from better use of acquirer's or targets assets. These include combining administration functions and the selling of the 'spare' head office buildings, using excess manufacturing capacity to generate high production volumes, combining distribution networks. The synergies can be measured using metrics such as return on capital employed (ROCE) or return on assets (ROA) (Creighton, 2013).

International bank M&A is motivated by size, the need to be big enough for the regional or global market. Next to size economies of scale and scope play the driving motive for M&A. Economies of scope are the predominant motive for domestic conglomeration. The rationale is to provide 'one-stop shopping' of different financial products to the target consumer. In addition, revenue expanding is the main driving factor to M&A. The major reasons for international conglomeration are economies of scope and size, to be attractive to the larger international market (European Central Bank, 2000).

2. Diversification: Diversification is buying firms beyond a company's current line of business in order to create financial synergy. The new product lines or target markets may be related or unrelated to the firm's current products or markets. A firm may attempt to achieve higher growth rate by selling its current products in new markets that are unfamiliar or may try to acquire a new product (DePamphilis, 2017). During the 1970s and early 1980s strategic planners were caught in expansion fever. Big was beautiful and everyone wanted to get bigger and expand their business portfolio. Diversification is defined as enabling the company to sell new products in new markets. This means in an acquisition the target company operates in a business unrelated to the other firm. The diversification factor was one of the major reasons to the third wave of M&As. The principle behind diversification is "putting one's egg in one basket" may not always be wise. A company losing customers due to shift to substitute products may look for diversification by acquiring the company with substitute products (Larsson & Wallenberg, 2002).

3. Strategic realignment: Firms make rapid adjustments to changes in their external environment like regulatory changes and technological innovations through M&A. Industries that have been subject to significant deregulation have been at the center of M&A activity. Deregulation breaks

down artificial barriers and stimulates competition. Firms that have been highly regulated often are unable to compete successfully following deregulation and become targets of strong competitors. Therefore, deregulation sparks flurry of M&A activities which leads to a lower number of competitors. When a company wants to get into another country's market it is often easier cooperate with or buy an already existing business. One of the main reasons to merge during the latest wave seems to be to get access. Businesses are acquiring others in different countries to gain access to new markets for their existing products, to R&D, technology, distribution channel, low cost of labor or manufacturing operations (DePamphilis, 2017; Larsson & Wallenberg, 2002).

Technological advances create new products and industries which enforces radical restructuring of existing ones. Existing firms may become obsolete in their products and markets. To combat such challenges firms, restructure their products strategically (DePamphilis, 2017).

4. Stagnation: Unsatisfactory growth rate, is likely to occur as an industry reaches its stage of maturity. In order to achieve a renewed growth merger is defensive strategy in time of stagnation and bad profitability. Greater resources and increased market shares give the companies a stronger market position and increased external efficiency.

5. Hubris and the "winners curse" Managers with successful M&A track records may pay more than what the target is worth due to over confidence. CEO having over paid may feel remorse at having done so, and experience what has come to be called the "Winners curse" (DePamphilis, 2017).

6. Buying under-valued assets: the Q-ratio Firms choose to invest in new and equipment or try to obtain the asset by buying a company with a market value less than what it would cost to replace the assets (DePamphilis, 2017).

7. Managerialism (Agency problem): Agency problem arises when the interests of current managers and the firm's shareholders differ. Managers of the acquiring firm make the strategies and acquisition decisions They make M&A to add to their prestige, build their spheres of influence, augment their compensation or for self-preservation. Agency problem is prominent with younger CEO. Agency problems typically arise when management owns a small proportion of share capital. Agency problems that drive M&A are related to wage, status and power as well as job security. There is a stronger link between firm size and larger rewards. M&A significantly increases the CEO compensation. Being in charge of a larger firm and receiving a higher compensation is related to status and power. Job security is also positively related with firm size (DePamphilis, 2017; Thanou & Daskalakis, 2013).

8. Replacing Management: Managers try to maximize shareholder value by either replacing inefficient management in the target firm. Some mergers are triggered by the belief that the acquiring firm's management can better manage the target's resources (Larsson & Wallenberg, 2002) Inefficient management can exist for a limited period of time, but over the long run, the market mechanism ensures that they are replaced. Mergers are seen as an economical way to eliminate bad management. Troubled or underperforming banks are often taken over as a better alternative to bankruptcy. Acquiring banks has realized higher performance when they absorb under- performing targets which suggests that that mergers are more beneficial to acquiring banks when the performance gap between targets and acquirers is wide (Awdeh & EL-Moussawi, 2011). Inefficient management hypothesis argues that firms led by weaker managers

will be undervalued and become a potential target to potential acquirers (Thanou & Daskalakis, 2013).

9. Tax consideration: Taxes influence corporate decision making. Acquirers of firms with accumulated losses and tax credits may use them to offset future profits generated by combined firms. Companies whose headquarter reside in high tax countries may prefer to M&A a company which exists in a favorable – tax country to move its headquarter to the favorable tax country.

10. Increasing market share /market power: Mergers could increase the market share of consolidated banks which may increase their market power. Market power is referred to as monopoly power and it is the ability to set and maintain price above competitive levels. Mergers tend to reduce competition which leads to higher profit gain from higher prices. In addition, being market leader brings advantages of pricing power and cost economics (Awdeh & EL-Moussawi, 2011).

11. Entry to new markets: The easiest and fastest way to enter a new market could be through the acquisition of an existing ‘player’. Banks that have reached the practical limits of expansion in their home markets entering a new market is the motive for M&As. Institutions located in markets with little potential for growth if they need to grow larger to remain competitive as well as if they want to extend their activities in order to provide services to their home country clients in international transactions triggers the process of M&As. Increased market power is achieved by product differentiation, barriers to entry and market share (Thanou & Daskalakis, 2013 ;Awdeh & EL-Moussawi, 2011).

12. Avoid banking crisis: When the banking sector is relatively healthy, there is no urgency for policy makers to take actions to strengthen the banking sector. When the bank sector or

individual bank is under severe pressure, interventional measures are inevitable. Policy makers enforce banks to undergo M&As rather than bankruptcy and liquidation which are costly for individual banks and the entire banking system. In the U.S. the wave of bank failures in early 1980s triggered a wave of bank M&As to avoid the liquidation of a large number of failed banks. Thus the trend of bank M&As in the U.S. was driven by market forces that have found consolidation a way to stop the collapse of more banks, at the same time by regulators who aimed at avoiding banks failures (Awdeh & EL-Moussawi, 2011).

2.3 Phases and Process of M&A

Most M&A are friendly deals in which two companies negotiate the terms of the deal. Communication between senior management of the two companies is started and they try to work out the pricing and other terms of the deal. For public enterprises, once the terms of the deal have been agreed upon, it is presented to the shareholders of the target company for their approval. Larger deals may require the approval of the shareholders of both companies. After shareholders' approval the process moves forward for a closing. Public companies have to do public filings for major corporate events and the sale of the company is obvious thereafter.

In a hostile deal the takeover process is different. Instead of direct communication there is an odd communication process that involves attorneys and the courts. Bidders try to meet shareholders directly to convince them accept their own terms, against the will of the top management. Target companies go a great length to avoid the takeover (Gaughan, 2005).

Corporate restructuring refers to the changes in ownership, business mix, asset mix and alliances with a view to increase the shareholder value. It includes a wide array of activities such as mergers, acquisitions, joint venture, spin-offs, leveraged buy-outs, demergers, buyback of shares,

capital reorganization and sale of business units and assets. Among these, mergers and acquisitions are the most common route taken by corporations for inorganic growth all over the world. Various parties are involved in M&A deals. These are business owners who are searching for potential partners, investment bankers who are responsible for managing the M&A, lawyers who provide advisory service, regulatory authorities who are concerned about the operations and safety of the capital market and increasing corporate dominance in the economy and academicians who want understand M&A better.

- 1 Run up: it includes the period of deal making up to the announcement of the merger. People who involved in this period are deal makers, typically chief executive, financial and legal experts and a range of advisors. The main activity at this stage is assessing the value of the deal. Due diligence: is a stage where the acquirer assesses the value of the human resource. It audits the numbers and roles of staff together with compensation details. Culture audits: understanding the culture of the member organization is very important to deter failure of the M&A
- 2 The transition: It is the period following days of the merger. The major characteristics of this period are: widespread anxiety, suspicion, preoccupation with new appointments and heightened response to every nuance.
- 3 Communication: the key principle in re-establishing trust and providing accurate information to people to manage their emotional responses.
- 4 The integration: it is determined by how much integration is required and how much of the organization is involved. The goals of integration are knowledge building, credibility building and behavioral building.

- 5 Staff retention: when the value of a company relies on the knowledge of its employees' it needs to re-assess their position in the new organization.
- 6 Cultural integration: mergers fail due to unresolved cultural issues. When two companies merge people of different background are obliged to co-operate. The M&A process should assess the organization, professional and national cultures in order to harmonize the people of the new organization (Garrow & Holbeche, 2000).

2.4 Types of Merger and Acquisition

Mergers can be classified in to three broad categories.

1 Horizontal merger: It happens when companies with same or closely related product in the same geographical area (market) perform merger. It can affect the level of competition in an industry. Normally competition benefits consumers by offering lowers prices and greater output being put on the market. By doing so horizontal mergers decrease the level of competition by reducing the level of competition and increasing the monopoly of the market by fewer giant companies. As a result, to keep consumers welfare most nation have laws that help prevent the domination of an industry by few competitors. Such laws are called antitrust laws in U.S and competition policy outside of U.S (Gaughan, 2005 (Garrow & Holbeche, 2000). Horizontal mergers may increase the market power of the combined firm and enable it to extract monopoly rents. Managers may be focused for mergers based on their own self-interest. They may be interested in mergers to maximize firm size instead of shareholder value. Maximizing firm size increases job security because a hostile takeover is less likely in a large and rapidly growing firms. This increases bidder manager's own power, status and salaries create more opportunities for lower and middle level managers at bidding firm. It can also be defined as ownership or increased control over competitors. It is characterized by the merge or acquisition of the

competitor. In case of large firms this strategy may violate the competition act. Horizontal integration which includes the acquisition of a competitor and the introduction of new products and services. The new unit is fully integrated to the existing company. Horizontal mergers lead to industry concentration. Industry concentration is defined as the percentage of total industry activity measured by total revenues that are controlled by the largest companies. The greater the amount controlled by a smaller number of companies, the more concentrated the companies. Most horizontal combinations do not result in an outright monopoly but in increased concentration of the industry and oligopolistic market structure. Monopoly power is not exercised in a more concentrated sector, several large competitors, as each of the companies may have lower economic and financial costs. This behavior leads to the reduction on the prices of products and services competitively to consumers (Chandrashekar, 2008; Garrow & Holbeche, 2000; Larsson & Wallenberg, 2002).

2 vertical mergers: Vertical merges happens when organization involved in M&A have a buyer-seller relationship prior to combination (Garrow & Holbeche, 2000). Vertical mergers are deals between companies that have a buyer and seller relationship with each other. A company might acquire a supplier or a closes company in the distribution chain to consumers. A manufacturer and distribution agent may sign a deal which is a good example of vertical mergers. It is defined as the company's business scale expansion incorporating the activities of suppliers and customers. It can be of two type. Backward integration is the acquisition or ownership of the company increased control over supply. Forward integration is the control over distributors and resellers. It includes the purchase of a distribution system or to set up such system internally. The potential benefits of vertical integration include cost savings, cost avoidance in the market, quality control and applied technology. If there is uneven flow of resources, company's existence

is threatened and leads to vertical integration. The main benefit of backward integration is enhanced and dependable access to supply of resources whereas forward integration leads to strong marketing and retail capability (Garrow & Holbeche, 2000; Larsson & Wallenberg, 2002).

3 conglomerates: These are combination of companies that do not have a business relationship with each other. they do not have buyer-seller relationship and are not competitors. Conglomerates were common in the 1960 s when antitrust enforcement prevents companies from vertical or horizontal mergers. It uses strategies of product extension, market extension and unrelated acquisition. Product extension is when the variety of products increases but the products are not competing directly with one another. Whereas market extension is a strategy where the firm is producing the same products and services but in different market areas. Unrelated acquisition is when the parties undergoing M&A are unrelated in products and services. Such strategies include a category for which there are no obvious technological or marketing synergies or cross-selling opportunities exist. Unrelated diversification can bring greater benefits than the related diversification (Garrow & Holbeche, 2000; Garrow & Holbeche, 2000).

4. Concentric diversification: means providing something new but related product to the company's existing product line. The new products technologic and marketing aspects are in synergic position with the company's current production.

2.5 Theories of M&A

A theory is a generalized statement of abstraction or ideas that asserts, explains or predicts relationships or connections between or among phenomena within the limits of critical bounding assumptions that the theory explicitly explains. A theory on the other hand can be explained as a

set of interrelated constructs (concepts), definitions and propositions that present a systematic view of phenomena by specifying relations among variables with the purpose of explaining or predicting the phenomena (Kivunja, 2018). A theory highlights and explains something that one would otherwise not see, or would find puzzling often, it is an answer to 'why' question. Theories are composed of one or more hypotheses each of which consists of concepts linked by relationships. Theory must be capable of being tested and either confirmed true or falsified. A theory needs to be able to cover a range of settings (Gilbert, 2008). A theory is a logically connected system of general propositions, which establishes a relationship between two or more variables. It is also an explanation of a particular social phenomena (Abend, 2008).

Good theory provides a framework of analysis for operational management since it provides structure for where difference of opinion exists. The goal of a good theory is a clear explanation of how and why specific relationships leads to specific events. The primary goal of a theory is to answer the question of how, when (where) and why unlike the goal of description which is to answer the question of what (who) (Wacker, 1998). Theories are speculative answers to perceived problems and are tested by observation and experiment. The truth of a theory can be confirmed to be true or it can be falsified and totally rejected by making observation which are inconsistent with its statements. In this way science proceeds by trial and error. When one theory is rejected another is proposed and tested and the fittest theory survives. For a theory to be tested it must be expressed as a statement called hypotheses (Walliiman, 2011). A theory needs to be tested, to do so there must be a method of measuring each concept. For each concept there must be an indicator. An indicator is a method of measurement that aims to measure the concept accurately. Indicator should be valid, accurately measure the concept, and reliable, measurement should be consistent from one to the next (Gilbert, 2008).

Theory is important for researchers and practitioners since it provides a framework for analysis, it provides an efficient method for field development and it provides clear explanation for the pragmatic world. Theory development reduces errors in problem solving by building upon a current theory. Building upon a current theory is equivalent to incorporating all that is known from the current literature into a single, integrated, consistent body of knowledge. For researchers. Using a single integrated body of knowledge for analytical and empirical testing gives the results a deeper theoretical meaning by differentiating between competing theories (Wacker, 1998).

A number of theories have been applied to explain M&A.

Efficiency theory: suggests that mergers are planned and it will only occur when they are expected to generate enough realizable synergies to make the deal beneficial to the parties, the bidder and the target. According to this theory the main motive of M&A is to gain synergy (operating or financial). The synergies may be in the form of reduction in cost or increase in revenue. Efficiency theory states that mergers are carried out to achieve synergy, thereby benefitting the shareholders of the company (Pol, 2020; Soundarya et al., 2019). Many co It also Explains that M&A are conducted to bring efficiency to the firm. Efficiency is enhanced by taking advantage of specialized skills or target management, eliminating the idle resources, sharing expensive technologies between the acquirer and the target, reducing transaction costs and reallocating existing expenses. It suggests that mergers occur since two firms have different strengths and weaknesses and different efficiency levels. It is also called differential efficiency theory. Through merger the efficiency of management of one company is transferred to the inefficient company management firm which results in social and private gains because it not

only improves performance but also saves resources of the company. It is the basis of horizontal mergers (Weitzel & McCarthy, 2011).

Inefficient management theory: it is another variant of efficiency theory. It suggests M&A increases efficiency of a company by removing inefficient management. It is the basis of unrelated mergers (Weitzel & McCarthy, 2011).

Resource dependent theory (RDT): is an explanation of how the external resources like skilled worker, money technology, and raw materials of an organization affect the behavior of the said organization. Resources of a firm consists of tangible assets, which are put to produce productive services planned by the firm. RDT explains the impact of social action and organizational changes towards an organization. RDT offers an externally focused perspective of why an organization might acquire or merge with another organization (Ullah & Seman, 2021).

Monopoly theory: M&A are executed to increase market power market power thereby transferring wealth from the customer to the acquirer. It means expansion in terms of either geography or product range or both. It has attached benefits like reputational capital and demand for diversification by managers and employees. It helps increase the corporate debt capacity and decrease the present value of future tax liability (Rohra & Chawla, 2015; Weitzel & McCarthy, 2011).

Empire building theory: Claims managers go for M&A to achieve their own personal goals rather than maximizing the wealth of shareholders.

Raider theory: Involves benefiting the shareholders of acquiring firm at the cost of shareholders of the target firm.

Process theory: explains that mergers are carried out on the basis of outcomes of various processes. Managers may need expertise, knowledge on uncertainty and political pressure as well as planning.

Valuation theory: managers undergo M&A when they have better information about the value of the target company than the stock market in order to get benefits to the firm.

Disturbance theory: It states that M&A are the results of economic disturbances like oil crisis.

Strategic realignment theory: Economic environment is dynamic in nature. Companies need to realize their strategies depending on changes in the economic environment. The changing and uncertain business environment is also another reason for mergers. M&A happen due to strategic realignment to changing environment.

Information and signaling theory: states that two different investors behave differently when they have different information. The merger announcement is a source of information and signal to market participants about the possible impact of deal on firm value (Rohra & Chawla, 2015).

Agency and behavioral theory:

Agency problem occurs when there is a conflict of interest between agents of the firm, the managers, and principals of the firm, the shareholders. A manager is representative of the firm and the shareholders. A manager who owns less percentage of shares gives less time to the company's wealth-creation activities. It would be costly for the owners of the organization to supervise managerial activities since it demands larger resources in the form of incentives. To retain the interest of shareholders a firm separates the ownership and control rights from managers. So that if managers need to make decision of M&A deals, they need the approval of shareholders (Weitzel & McCarthy, 2011). Managers have a substantial control in modern

corporations. Managers seek to acquire other firms in order to serve their own personal economic gains and do not look to the best solution for the firm. The pride of managers makes them to believe that their valuation is superior to the valuation determined by the objective market. Managers ignore the shareholder value like growth or empire building in favor of their own personal interest. They pursue their own goals at the expense of shareholders. The threat of financial distress and bankruptcy is greater on the managers than the shareholders. Hence managers undertake M&A assuming that the greater size of the company might grant immunity of being taken over (Larsson & Wallenberg, 2002). A takeover is an external control device to the agency problems. Takeover enables outside managers to control decision process of the target firm by bypassing the existing managers and board of directors. A merger as a takeover threat act as a control mechanism as it is viewed firm's performance is poor due to inefficient managers. This leads to removal of inefficient management. Agency Theory: argues that managers have incentives to ensure their firm grow beyond their size. A large size of a firm leads managers to control large amount of resources. The growth leads to increased compensation for managers. As a result, managers usually resort to mergers in order to achieve their own personal gains without any consideration of economic reasons (Fatty, n.d.; Weitzel & McCarthy, 2011)

According to (Sarika & Vasantha, 2018) two schools of theory for bank M&A are the neo-classical, and agency and behavioral theory

Neoclassical theory: Focuses on the relative worth of tangible or physical capital assets to firms at different points in time. In the neo classical theory decision of M&A are made to please the shareholders of the firm. In this view shareholders interest is superior to the interest of managers (Larsson & Wallenberg, 2002; Sarika & Vasantha, 2018). While agency and behavioral theory

states that managers deliberately look for merger and acquisitions to achieve their own personal benefit targets on the cost of shareholders interest.

(Weitzel & McCarthy, 2011) have classified the theories of M&A in to two broad categories. These are Value increasing theory and Value decreasing theories; value increasing theory and the value decreasing theory.

1. Value increasing theory: according to this theory M&A occur because they generate 'synergies' between the acquirer and the target. Value increasing theory is divided in to different sub-theories of the following;

a. Efficiency theory: claims that mergers will only occur when they are expected to generate enough realizable synergies to make the deal beneficial to both parties. It predicts value creation with positive returns to both the acquirer and the target. Most literatures conclude operating synergies are the more significant source of gains.

b. Market power theory: mergers happen to increase the market power of dealers.

c. Theory of corporate control: It explains that management wishes to acquire an underperforming firm, to remove those managers who have failed to capitalize on the opportunities to create synergies.

2. Value destroying theories: Such motives lead to failure to create value and M&A activity becomes detrimental. Different literatures of M&A revealed that somewhat 60 – 80% of M&A deals are failed. The sub-theories under value destroying theory are;

- a. Theory of managerial hubris: Managers become overconfident, overestimate their abilities to create synergies, and the probability of overpaying is increased. This increases the chance of failure of the deal and leads to “winners-curse”.
- b. Theory of managerial discretion: This theory explains firms whose internal funds are in excess of the investments required to fund positive net present value projects, are more likely to undergo strategic decisions like M&As. High level of liquidity increase managerial discretion, making managers to pay for non-good mergers when the goods are lost. When there is increased cash flow (FCF) managerial discretion also increases.
- c. Theory of managerial entrenchment: claims that M&As are undergone not to increase the value of shareholders but to preserve their personal interests. Managers make investments to reduce the risk of replacement. Entrenchment is not only pursued for job security itself but also to extract more wealth, power, reputation, and fame.
- d. Theory of empire building: managers are explicitly motivated to invest to invest in the growth of their firm revenue or asset base (Weitzel & McCarthy, 2011).

2.6 Empirical Evidence on Mergers and Acquisition

Since 1991 the global banking sector have been in the process of transformation and consolidation. Deregulation, globalization of economies coupled with technological development has changed the banking sector landscape dramatically. In order to cope up with the changing environment, the banking sector is resorting to the process of consolidation, corporate restructuring and strengthening to remain efficient and viable. External factors that trigger M&A deals are deregulation and laws, globalization, technological progress and economic conditions are the main ones. Internal triggers of M&A are synergy, agency-managerial problem and hubris

are critical ones (Sarika & Vasantha, 2018). The fundamental role of merger activities is to enable companies to adjust more efficiently to new challenges and opportunities. Majorities of the world's great amount of organization exist out of economic reasons i.e. it serves its owners with some profit even if there are many motives behind M&A deals the ultimate goal beneath each motive is economic gains of the company. Forces that drive M&A activity can be classified as either explicit or implicit. The explicit motives are the reasons actually given by company management. The implicit motives refer to reasons that can be suspected, but are not confirmed by managers (Larsson & Wallenberg, 2002).

A merger may have single or several reasons. The main motive of bank merger and acquisition is to maximize shareholder value. This can be achieved by increasing a bank's market power, efficiency and risk diversification. Efficiency is improved when a strong bank acquires a weak, poorly managed bank (Sarika & Vasantha, 2018). Among the many reasons as to why mergers are undertaken is the speculation on the stock market that the value of a firm increases through rumors of an imminent mergers. Statements made by journalists and experts on different forms of media are tempting to undergo M&A. An analyst in an acknowledge financial papers claim that mergers or acquisitions are successful and made glorified. This claim is appealing to many companies and are inspired to execute M&A. Companies at this point, eager to reap the same gains as their fellow competitors, make a hasten observation as to whom to collaborate and make erroneous decision. There by most companies are exposed to failure due to M&A. Medias make an individual to apprehend a specific aspect of life and at the same time offer an interpretation (Larsson & Wallenberg, 2002).

A journalist reporting on merger or acquisition states facts at the same time, deliberate or not, make judgments, on the issue. The reader will not go further to interpret by him/herself and get

imposed by the journal interpretation. The more equal in size and power the two combining firms, the more likely the deal is merger. Whereas the more one part of a purchase is dominant the more likely the deal is an acquisition. The reason why one financial institution merged with another institution is due to rational and drivers. Rational indicates strategic implementation whereas drivers indicate control of capacity from the economy. Factors that motivate M&A are categorized as shareholder wealth maximization goal, managerial self interest and other factors which contribute to the conducive environment for M&A (Larsson & Wallenberg, 2002; Ullah & Seman, 2021).

Of the approximately 7600 commercial banks in the U.S. a substantial number has disappeared as independent entities by 2003. The vast majority of reduction was due to M&A. Less profitable and inefficient firms are more likely to be acquired. An acquisition occurs when there is a change in control. A large bank is less likely to be acquired by small acquirers, the greater its size it is more likely to be acquired by larger acquirers (Hannan & Pilloff, 2009). It analyses 3520 M&A deals of 20 years duration (1984 – 2004). They found that single motive acquisitions are relatively uncommon. About 80% of merger and acquisitions deals have multiple motives. They have found that market timing, hubris or agency problem, synergy and response to industry or economic shocks are the motivation behind M&A deals. In 1955, completed mergers and acquisition among corporations in the U.S. reached an aggregate value of US \$ 377 billion. In 2005 the aggregate value of M&A deals reached US \$ 1.1 trillion (Nguyen et al., 2012). Most M&A activity in the EU has had a domestic focus and has involved smaller targets, with larger and sounder acquirers acting as consolidators. Consolidation seems to have had a moderately positive impact on the profitability of EU banks involved. The Euro area banking market become increasingly concentrated and a third of its banking groups, mainly the smallest banks, have

disappeared since the global financial crisis. The efficiency and stability of the banking system would benefit from further consolidation and it should be driven by market forces (Figueiras et al., 2021).

In developed nations, market forces trigger M&A operations, where as in emerging markets the monetary authorities play a major role in bank M&A. M&A is an exit mechanism when banks face systemic crisis in developing countries. Many studies have revealed M&A of banks in emerging markets are guided and directed by the authorities and market forces are absent in the process. In Lebanese banking sector in 1980's, following deregulation policy, there was proliferation of large number of undercapitalized and inefficient banks. The government of Lebanon then declared obligatory directive that "pushes" banks to undergo M&A. by setting tighter capital requirements. In addition, the directive restricts new branch opening to only two per year, that triggers acquisition of small banks by larger banks. Twenty-five bank mergers were recorded under the law of bank mergers between 1994 and 2002. Smaller banks facing tough capital requirements and the increasingly competitive environment accepted takeover bids. In emerging markets, authorities interfere directly in bank M&As. They tend to encourage and support efficient and healthy banks to acquire underperforming and unstable banks. In Central Europe strong banks were forced to absorb weaker ones to ensure the stability of the national bank system (Awdeh & EL-Moussawi, 2011). Banking mergers and acquisitions are aimed at amplifying efficiency, enhancing competitive advantage, achieving synergy and improving shareholder's value. But it is found that after M&As there is no important difference in the performance of banks when pre and post-merger performance are compared. The driving forces of domestic consolidation is cost saving through economies of scale. In the EU the ratio of

domestic to cross-border bank mergers were five to one over the year 1990 – 2001 (Fatty, n.d.; Larsson & Wallenberg, 2002; Shangquan, 2000).

Government-driven consolidation is usually limited by the authorities and allows M&As of mostly domestic banks. Guided M&As with foreign banks were observed at the early stages of foreign bank entry liberalization. Market driven consolidation of banks can lead to transnational M&A resulting in creation of large financial institution of world importance. Consolidation of banking sector in S. Korea was performed by state authorities in the 1990's. By the end of 1999 the total number of banks were reduced from twenty-seven to seventeen. Thailand, Philippines and Malaysia have consolidated their banks slowly through the help of more of market forces. Market driven consolidation is relatively new type of banking consolidation in the last 20 years (Mohamadi & Bohma, 2017). After studying M&A deals from 1991 – 2011 fourteen banks among total of 38 banks has undergone M&A deals. They found that raising shareholder equity, increasing revenue and strengthening financial position, to diversify products and services were significant internal motives that drive M&A. Economic, legal, political, technological and competitive forces were external motives to undergo M&A deals (Smirnova, 2014). 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). After studying 150 large Slovenian companies for M&A it is found that synergy by sharing activities (62.5%), entering new market fast (56.25%), low valuation of firm (31.5%), financial synergy, and excess cash flow are the most significant motives that determine acquisition. Tax motives and megalomania and self-fulfillment are less important factors in the acquisition deals. Strategic realignment to fit the changing environment

is the factor that determine the acquisition strategy in Slovenia but not as strong as could be expected (Lahovnik, 2016).

A study on the motives of M&A deals in small and medium enterprises (SME), in the European context SMEs comprise of 99% of all firms in the economy. At global levels SME may contribute between 40 – 60% of national GDP. Their result showed that the conduct and financial success of M&A by entrepreneurial enterprises is significantly different to the large public firms. (Weitzel & McCarthy, 2011) Studies in the EU have found that there is no single rationale that motivates M&As. Studies focused in 1990 – 2000s indicate mergers are often aimed at improving profitability and efficiency. Cross border mergers were found to occur more frequently when countries are closely linked by a common language or trade. European studies support that smaller banks are more likely to be acquired. Gaining market power and diversification of revenues are other motives of mergers. Cross-border transactions are also likely to follow existing financial links and emerge with in clusters of Euro area countries (Figueiras et al., 2021).

Analysis of data from the U.S. banking sector has revealed that there is a direct and positive performance in banking productivity, profitability as well as shareholder values after M&A. Some studies have shown M&A has less importance impact on the bank operational performance. Acquisition often have a negative impact on employees' behavior resulting in counter- productive practices absenteeism, low morale and job satisfaction. Efficient and strong financial institutions tend to broaden their market or maneuver beyond national boarder. This can be accomplished by foreign direct investment (FDI) which comes with two approaches namely green filled investment and new operation procurement. New operation procurement approach might involve cross boarder M&A. Studying 20 years of M&A deals in the European public

utility, from 1991 – 2012, synergy motive is significant factor for M&A deals in the public utility sector. They studied a total of 172 M&A deals (Brahma et al., 2018; Ullah & Seman, 2021).

Regarding FDI, in general, and M&A, in particular the factors that moderate in the continent Africa are not well studied. Prior research in Africa has been focused on exploring factors driving inward FDI not on M&A. M&A in Africa can bolster economic development by improving local business capabilities, creating an international presence for local companies, providing access to global markets, providing financing for the growth and generating the level of market competition necessary to spur efficiency in local companies. Several African companies have a low record of M&A activities historically, too poor financial reporting quality and low investor protection. Countries with better accounting standards and stronger shareholder protection have a higher volume of M&A in Africa. The most active M&A activities are recorded in financial services (banking, insurance). Among 2,212 financial firms, there were 78 targets. The study covered fifteen African listed firms (Abongeh et al., 2016).

2.7 Conclusion and Literature Gap

Developed countries have well developed M&A process. All M&A activities are well recorded and researchers have ample data source to conduct study on the factors that motivate M&A activity. Ethiopia's financial system is not liberalized and M&A activities between private commercial banks has not yet recorded. As the national Bank of Ethiopia raised the paid-up capital requirement required to establish banks and the probability of entry of foreign banks to the country in the near future will tighten the competition among commercial banks. Among the strategies that private commercial banks will employ to survive the competition will be M&A. So far there is no study that investigated what factors really trigger M&A activity between

private commercial banks. This study will try to investigate the factors that necessitate M&A of private commercial banks in Ethiopia.

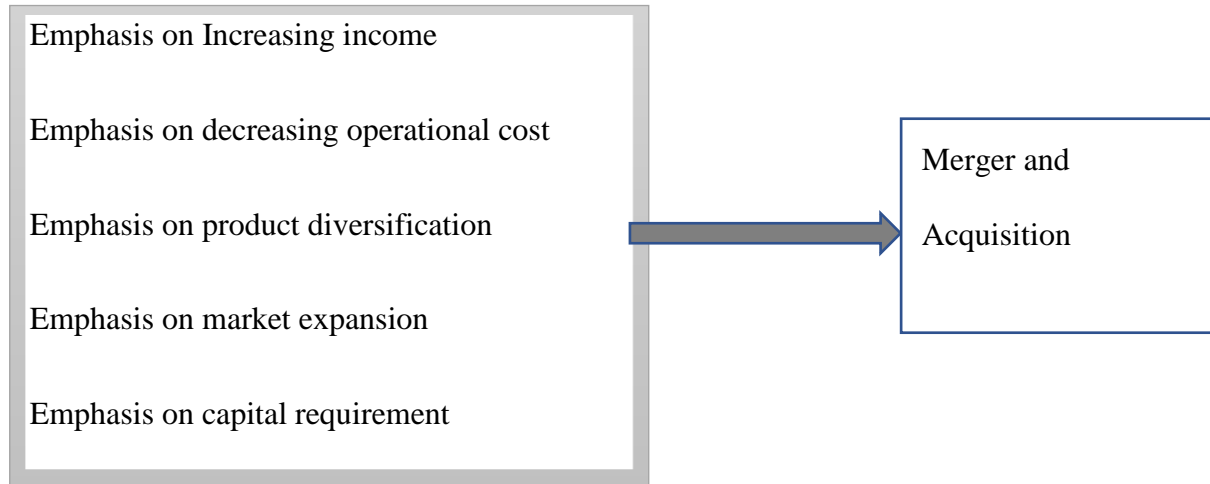


Figure 2. 1: Conceptual frame work

CHAPTER THREE

RESEARCH METHODS

3.1 Introduction

Knowing is one of the most specific human processes and knowledge is its result. Knowledge and knowing have been subjects of human inquiry since ancient times. There have been many Theories and explanation of knowledge yet none of them are satisfactory. The most accepted definition of knowledge is “justified true belief”. Knowledge is a universal concept which attracted the attention of philosophers. Knowledge is an abstract concept without any reference to the tangible world. It is very powerful concept, yet it has no clear definition (Bolisani & Bratianu, 2018).

There are different views on how we understand the reality around us. Metaphysics is field of philosophy concerned with questions like what is to be, who we are, what is knowledge, what are things, what is time and space. Idealism advocates that reality is all in the mind, that everything exists is in some way dependent on the activity of the mind. Eg. Music is not a sound, it is an emotional experience. Materialism advocates that only physical things and their interaction exist and that our minds and consciousness are wholly due to the active operations of materials. Hence phenomena are independent of social factors and are therefore stable. Eg Music is just vibration in the air (Walliiman, 2011).

There are two approaches as to how to acquire knowledge

Empiricism: claims that knowledge is gained by sensory experience (inductive reasoning).

According to this view ideas and forms cannot be separated from physical objects and sensory

information. Induction reasoning starts from specific observation or sensory experiences and then develops a general conclusion from them. It is the earliest and now the most popular form of scientific activity. We come to conclusion from what we have experienced and generalize from it.

Rationalism: advocates that knowledge is gained by reasoning (deductive reasoning). It justifies that our sensory experience plays no role. Deductive reasoning starts with the general statements and through logical argument comes to a specific conclusion (Walliiman, 2011).

The role of research in several fields of applied economics, whether related to business or the economy as a whole has greatly increased in time (C.R.Kothari, 2004). Research methodology is a way to systematically solve the research problem. It is a science of studying how scientific research is carried out. It has many dimensions and research methods constitute part of research methodology. When one talks about methodology, he/she not only talk about the research methods but also considers the logic behind the methods employed in studying the research problem and why other methods are not used so that results are capable of being evaluated either by the researcher himself or by others. Why research has been undertaken, how research problem is defined, in what way and why hypotheses is formulated, what data have been collected and what methods are employed, what particular techniques of analysis of data has been used and similar other questions are answered when we talk of research methodology (Walliiman, 2011).

3.2 Research Design

Decision regarding what, where, when, how much, by what means concerning an inquiry or a research study constitute a research design. It is the conceptual structure within which research is conducted. It constitutes the blue print of collection, measurement and analysis of data. The

design includes an outline of what the researcher will do from writing the hypotheses and operational implication to the final analysis of data. The overall research design is composed of the sampling design, observational design, the statistical design and the operational design. A research design must, at least, contain a clear statement of the research problem, procedures and techniques to be used for gathering information, the population to be studied and the methods to be used in processing and analyzing data. Research design has a great bearing on the reliability of the results arrived at and as such constitutes the firm foundation of the entire structure of the research work. A design which minimizes bias and maximizes the reliability of the data collected and analyzed is considered a good design (Walliiman, 2011).

There are different methods of research design. Hypothesis testing research are those where the researcher tests the hypotheses of causal relationship between variables. The selection of research design is dependent on research question; availability of data and the researchers own skills and preferences (Gilbert, 2008; Walliiman, 2011).

By the end of 2020/21 fiscal year there are seventeen private commercial banks operating throughout the country (National Bank Ethiopia, 2021). Merger and acquisitions are not common practice in any business sector in Ethiopia. As it is a rare practice, there is no research done on mergers and acquisitions by scholars. This study will be the first of its kind to find out the real motivators of M&A in the Ethiopian private banking sector. Currently, Ethiopia has no securities market. Besides to this, it has no well documented data on M&A activities that have taken place, if any. Although M&A is a widely discussed research topic in developed countries, information is limited in developing countries like Ethiopia. Explanatory research design will be employed. Explanatory research design explains why something occurs in the case of limited information. It

is a cause and effect relationship study where one is interested to study that causal relation is not robustly studied previously (George, 2022).

3.3 Research Approach

Research approach is a plan and procedure of a research that spans the steps from broad assumptions to detailed methods of data collection, analysis and interpretation. It is the plan or proposal to conduct research and it involves the intersection of philosophy, research design and specific methods. There are three broad research approaches. These are quantitative, qualitative and mixed approach of research. Quantitative research approach is an approach employed to test objective theories by examining the relationship among variables (W.Creswell, 2014). Variables can be measured on an instrument so that numbered data can be analyzed using statistical tools. In this study quantitative research approach is used.

3.4 Type and Source of Data

Data can be quantitative or qualitative type. Qualitative data are mostly non-numerical and usually descriptive or nominal in nature. It means that the data collected are in the form of words or sentences. Quantitative data includes measurement of something. It is numerical in nature and can be mathematically computed (Kabir, 2018). In this study the type of data is quantitative.

Primary data is the firsthand data gathered by the researcher himself. It is factual and original. It has not been published yet and is more reliable, authentic and objective. Primary data source provides direct or firsthand evidence about an event, object or person. Primary data source includes surveys, observation, experiments, questionnaire and interview. Secondary data is one that generated by large government institutions and business organizations as part of record and

report keeping. Secondary data source is an existing data collected for another purpose (Ajayi, 2017; Kabir, 2018).

The study used primary data and data source. The data is collected from Bank managers and senior banking officers using structured questionnaire.

3.5 Variables

A variable is an attribute of an object to be studied. In any research there are different types of variables. These are Binary, continuous, ordinal and nominal variables. Variables are also classified as dependent and independent variables

Independent variable is the one which is the cause of change. It is the variable which is altered in the study process and whose effect is observed and measured. In this research high paid up capital requirement, market expansion, operational cost minimization, product diversification, and income are the independent variables. The selection of the independent variables is focused on all possible factors within the domain of domestic banking system.

Dependent variable is the variable which is the outcome of the study. In this study merger and acquisition activity is the dependent variable.

3.6 Hypotheses

Hypothesis is the principal instrument in research. It is a set of propositions set forth as an explanation for the occurrence of some specified group of phenomena either asserted merely as a provisional conjecture to guide further investigation or accepted as highly probable in the light of established facts. A hypothesis should be clear and precise, capable of being tested, states a relationship between variables and should be consistent with most known facts. Hypothesis can

be stated as a null or alternate hypothesis. The null hypothesis is a prediction of no relationship between variables, designate as H_0 . Alternate hypothesis is initial hypothesis that predicts a relationship between variables exist, designated as H_a (Bevans, 2020; C.R.Kothari, 2004)..

There are five elements that threaten a company's business. These are intensity of rivalry, threat of new entrants, threat of substitutes and bargaining power of suppliers and customers. These all can be a sufficient argument for mergers. In order to reduce the bargaining power of suppliers and customers vertical merger is the best solution. In a vertical merger, the company is able to influence the prices of inputs and outputs and also further secure the inflow of resources from suppliers. (Fatty, n.d.; Larsson & Wallenberg, 2002; Shangquan, 2000).

The concept of risk diversification indicates that the integration of two firms can lower bank risk and reduce the probability of bank failure. The two common risk diversification mechanisms are product and geographic diversification. By product diversification risk may be reduced because the returns across different financial services industries may have lower correlation coefficient. Geographical diversification leads to risk reduction because loans and financial instruments issued in different location be low correlated (Thanou & Daskalakis, 2013).

H1: Emphasis on product diversification leads to merger and acquisition of commercial banks.

The importance of capital adequacy as a M&A motive is linked to the demand of financial regulators requirement of commercial banks to sustain a minimum capital adequacy ratio. The less capitalized banks are, the higher the probability to be acquired. Banks consolidate to reduce over capacity. Mergers and acquisitions are the main mechanisms for bank consolidations, as exit is near impossible in the regulated and protected banking sector. While many bank combinations are possible, supervisors are worry of large banks that are to big to fail.

Supervisors are reluctant to allow mergers that create mega banks with over €2.5 trillion – €3 trillion in assets. A merger among the top banks is likely to be blocked (Patty Duijm, 2018; Thanou & Daskalakis, 2013).

H2: Higher amount of capital requirement than by government regulatory body leads to merger and acquisition activity

The concept of coinsurance, imperfect correlation of business unit cash flows, allows resources to be transferred from cash-rich units to cash poor units as required. Target firms which are unable to finance their investment opportunities are said to be financially constrained. Such companies look for additional financing provided by an acquirer's unused borrowing capacity or excess cash balance as a form of financial synergy. Financial synergies arise when a high growth and a cash poor-firm is acquired by a cash-rich bidder (Chandrashekar Krishnamurti, 2008; DePamphilis, 2017). Financial synergy is the impact of corporate merger or acquisition on the cost of capital of the acquiring firm or the emerging entities. In financial markets, larger companies have advantages that may lower their cost of capital because they are considered less risky than smaller ones (Awdeh & EL-Moussawi, 2011).

H3: The demand to raise income triggers merger and acquisition activity.

Operating synergies between companies include products that enhance distribution of complementary product lines, lowering operating heads, improve economies scale and scope in product lines. It consists processes that are important determinants of shareholders wealth creation. The major source of operating synergy is the cost decline due to corporate pact (Chandrashekar Krishnamurti, 2008; Larsson & Wallenberg, 2002). Banking products require the utilization of costly resources such as branches, data processing systems, teller etc.

Economies of scale occurs when there is the ability to reduce cost per unit of output and the average cost of a product in the long run decreases as more units are produced. Large institutions have the ability to produce more services due to the use of technological innovations such as phone centers, ATM and e-banking, and at lower costs than traditional branching networks (Awdeh & EL-Moussawi, 2011). Such M&A are clearly related to cost reductions that are realized by cutting branch networks, staff and overheads in central office functions such as IT departments, macroeconomic departments and legal departments. M&A are also used to avoid takeovers. 'Large' bank M&A reflects repositioning of the institution involved. Increase in size reflects the perceived need to become big enough for domestic market. M&A offers the advantage to owners' optimization of the capital structure and the increase shareholder value (European Central Bank, 2000).

H4: The need to minimize operational cost can trigger merger and acquisition of commercial banks

Economic globalization refers to the increasing interdependence of world economies as a result of the growing scale of cross-border trade of commodities and services, flow of international capital and wide and rapid spread of technologies. It is an irreversible trend for the economic development in the whole world at the turn of the millennium. Multinational corporations (MNC) are the main carriers of economic globalization. Globalization of the financial sector has become the most rapidly developing and most influential aspect of economic globalization. International finance came into being to serve the needs of international trade and investment activities. Developed countries have been playing a dominant role in the process of economic globalization. In 1996, the total volume of exports of developed nations was U.S. \$ 4057 billion accounting 81.7% of the world's total value of international trade (Shangquan, 2000). A major

synergy for cross-border M&A is credit risk diversification. Another motive of cross-border mergers is client driven. A bank operating in a foreign country, lacking sophistication of systems that large corporates desire, are likely to undergo mergers (Patty Duijm, 2018). Market size, human capital, and efficiency opportunities are related to increase M&A volume. Governance quality has a positive relationship to increase M&A volume in Africa. As firm size increases so is its probability of being target for acquiring companies. It is inconsistent finding with the theoretical view that as size small so is being target for bidders. They also found Presence of an active stock market is a key ingredient in stimulating FDI through M&AS (Abongeh et al., 2016).

H5: The desire to expand market share of commercial banks can lead to merger and acquisition activity.

3.7 Population of the Study

The study population of this research is all private commercial banks operating in Ethiopia. The study is conducted using sample drawn from branches and head offices of private commercial banks located in Addis Ababa. The data is collected from managers and senior banking officers because the nature of the data to be collected demands experience in the field of banking sector.

3.8 Sampling Frame and Method

A complete enumeration of all items in the population is known as a census inquiry. A sample design is a definite plan for obtaining a sample from a given population. Sample design as well lay down the number of items to be included in the sample i.e. the size of the sample. For this reason, convenience (non-probability) sampling technique is used to select participants of the study. In this type of sampling the researcher gets the chance to select samples based on his own

judgement in such a way that it achieves to gather the desired data. The study is conducted by collecting data from private commercial banks officed in Addis Ababa, the capital of Ethiopia. The sample size refers to the number of items to be drawn from the population to be included in the sample item. Sample size is dependent on the nature of the study and availability of budget (C.R.Kothari, 2004). For each private commercial bank 15 questionnaire are administered. In this study 250 respondents were selected and the questionnaire were administered and a total of 200 questionnaires were collected.

3.9 Method 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. The goal of data collection is to capture quality evidence which translates to rich data analysis and allows the building of a convincing and credible answer to questions. 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).

In this study a structured questionnaire was prepared to collect the relevant data. The questionnaire is 5-scaled Likert type and respondent are expected to react to what levels of interest they agree or disagree to the points (measurements) raised on factors that lead to M&A.

3.10 Method of Data Analysis

The data is analyzed by employing inferential statistics. Since the data is quantitative and the questions administered is Likert scale, linear regression is the best way to make inductive inference about the population. Linear regression is a regression model that uses a straight line to describe the relationship between variables. It finds the line of best fit through data by searching the value of the regression coefficient(s) that minimizes the total error of the model. There are two main types of linear regression model; simple linear regression and multiple linear regression. Simple linear regression uses one variable whereas multiple linear regression uses two or more variables to explain the dependent variable (Bevans, 2020). The regression model assumed as:

$M\&A = \beta_0 + \beta_1 \text{ Income} + \beta_2 \text{ Product diversification} + \beta_3 \text{ Capital requirement} + \beta_4 \text{ Operational cost} + \beta_5 \text{ Market expansion}$. Where,

M&A = Mergers and acquisition

Product diversification = Desire to increase product diversification

Capital requirement = Raised paid up capital requirement by government authority

Operational cost = The need to minimize operational cost by commercial banks

Market expansion = The desire to expand market share by commercial banks

Income = The desire to increase income by managers

The tool used to analyze the data is SPSS software. The unit of analysis are private commercial banks.

CHAPTER FOUR

DATA PRESENTATION, ANALYSIS AND DISCUSSION

4.1 Descriptive Statistics of respondents

During the study a total of 200 questionnaires were distributed. The frequency distribution of the respondents and analysis of the result is carried out by using data from these respondents.

Table 4. 1: Frequency distribution of age of respondents

	Frequency	Percent
Male	119	59.5
Female	81	40.5
Total	200	100

Source: SPSS output of age distribution frequency

Among the total of 200 respondents of the study 81 (40.5%) are female respondents and 119 (59.5%) are male respondents.

Table 4. 2: Frequency distribution of level of education of respondents

	Frequency	Percent
BA Degree	105	52.5
MA Degree	95	47.5
Total	200	100.0

Source: SPSS output of frequency distribution of level of education of the respondents

As shown in table 2, 105 (52.5%) of the total respondents have Bachelor's Degree while the remaining 95 (47.5%) are MA Degree holders.

Table 4. 3: Frequency distribution of experience of the respondents

	Frequency	Percent
5-10 years	54	27.0
10-15 years	62	31.0
15-20 years	72	36.0
>20 years	12	6.0
Total	200	100

Source: SPSS output of the frequency distribution of experience of respondents

Analysis of the frequency distribution of experience of the respondents showed that 54 (27%) have 5-10 years of experience, 62 (31%) have 10-15 years of experience, 72 (36%) have 15-20 years of experience and the remaining 12 (6%) of the total respondents have > 20 years of experience

Table 4. 4: Frequency distribution of the current position of respondents

	Frequency	Percent
Bank manager	58	29.0
senior banking officer	142	71.0
Total	200	100.0

Source: SPSS output of the frequency distribution of position of the respondents

As depicted in the SPSS output table 58 (29%) of the respondents were managers and the remaining 142 (71%) were senior banking officers.

4.2 Descriptive statistics of variables

The typical Likert scale is a 5- or 7-point ordinal scale used by respondents to rate the degree to which they agree or disagree in a continuum (Sullivan & Artino, 2013). Kerlinger described a Likert scale as a summated rating scale where by an individual's score on the scale is a sum or average of the individual's response to the multiple items on the instrument. An alternative way of calculating a composite score of each individual is to calculate a mean – item summated score divided by the number of items constituting the scale in which the value falls in the continuum options (Warmbrod, 2014). Likert scale data at the ordinal level of measurement are best analyzed by using mode and median as a measure of central tendency and Chi-square test as analysis tool (Harry N. Boon, Deborah A, 2012). Once the composite score of Likert scale ordinal data is calculated then the mean becomes an interval scale. For interval scale measurement the mean is used as a measure of central tendency and standard deviation as a measure of variability.

The tables below depict the mean and standard deviation of the response of respondents on each question of the Likert scale. For a five-point Likert scale if the mean lies in the range 1-1.8 = strongly disagree, 1.81-2.6 = disagree, 2.61-3.4 = neutral, 3.41-4.2 = agree, 4.21-5 = strongly agree.

Table 4. 5: Descriptive statistics of results on emphasis on increasing income

	Minimum	Maximum	Mean	Std. Deviation
Merger and acquisition may increase the net interest income of banks.	1	5	4.05	.825
Merger and acquisition may increase the non-interest income (income resulting from deposits, fees, service charges, e.t c.) of banks.	2	5	4.07	.805
The need to use multiple sources of income (like banking, microfinance) can be introduced with the help of merger and acquisition.	1	5	4.06	.757
Merger and acquisition help to increase the customer activity (opening new bank accounts, banking transaction, deposits etc).	2	5	4.07	.848

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

Under the item emphasis on increasing income the questions “Merger and acquisition may increase the non- interest income (income resulting from deposits, fees, service charges, e.t c.) of banks” and “Merger and acquisition help to increase the customer activity (opening new bank accounts, banking transaction, deposits etc)” have a mean of 4.07 (i.e majority of the respondents agree) with a standard deviation of 0.805 and 0.848. Likewise, question “The need to use multiple sources of income (like banking, microfinance) can be introduced with the help of merger and acquisition” and “Merger and acquisition may increase the net interest income of

banks” the mean, 4.06 & 4.05, indicates that majority of the respondents have agreed with a standard deviation of 0.757 and 0.825 respectively.

For the question under emphasis on decreasing operational cost the mean of the response for each question lies in the range 3.41-4.2 which implies that majority of the respondents have replied “agree” for all questions raised with respective standard deviations as depicted in the table above.

Table 4. 6: Descriptive statistics of results on emphasis on decreasing operational cost

	Minimum	Maximum	Mean	Std. Deviation
Merger and acquisition help minimize the duplication of banking activities.	1	5	4.09	.858
Merger and acquisition eliminate branch overlapping.	1	5	4.03	.736
Banks under go merger and acquisition in order to reduce unnecessary managerial as well as operational positions.	2	5	4.08	.826
Providing more services using fixed set of premises can be obtained through merger and acquisition.	1	5	4.09	.843

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

For the question included under emphasis on product diversification the mean of the responses for all four questions lies in the range 1.8-2.6 which implies that majority of the respondents

have replied “neutral”. The standard deviation of the mean of the responses for all questions are provided along with the mean in the table above.

Table 4. 7: Descriptive statistics of results on emphasis on emphasis on product diversification

	Minimum	Maximum	Mean	Std. Deviation
Merger and acquisition are done in order to provide different types of products/services to customers	1	5	2.55	1.155
Merger and acquisition are performed for the sake of managing financial complexities	1	5	2.40	.940
Merger and acquisition have role in creating portfolio of banks’ products/services.	1	5	2.30	1.051
In order to minimize market risk, merger and acquisition is performed by banks as a part of related diversification	1	5	2.11	1.050

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

Table 4. 8: Descriptive statistics of results on emphasis on market expansion

	Minimum	Maximum	Mean	Std. Deviation
In order to obtain power and exclude rivals, banks go through merger and acquisition.	2	5	4.09	.741
Merger and acquisition have roles to capture market share.	2	5	4.23	.806
Merger and acquisition are effective tools for eliminating competition.	2	5	4.11	.817
Merger and acquisition make it easier for companies to obtain better market by increasing its size.	1	5	4.05	.755
In order to achieve success in key area of operations, merger is done with banks having deeper market penetration	2	5	4.15	.790

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

The descriptive statistics of the results under the item emphasis on market expansion the second question “Merger and acquisition have roles to capture market share” has score of the mean 4.23, with a standard deviation of 0.806, lies in the range 4.2-5. This indicates that majority of the respondents replied “strongly agree”. The mean of the remaining questions lies in the range 3.41-4.2 with respective standard deviation. The mean indicates that majority of the respondents have agreed with the concepts.

Table 4. 9: Descriptive statistics of results on emphasis on maintaining capital requirement by NBE

	Minimum	Maximum	Mean	Std. Deviation
The new minimum paid-up capital requirement (5 billion ETB) to start banking business will trigger merger and acquisition	1	5	4.14	.777
Going for merger and acquisition is easier than issuing new shares for banks to achieve the new capital requirement	1	5	4.10	.860
Merger and acquisition help banks having trouble with minimum paid-up capital requirement	2	5	4.11	.819
Providing longer period of time (5 years) to increase banks paid-up capital by NBE will not trigger merger and acquisition of banks.	1	5	2.10	1.022

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

Under the item on emphasis on maintaining capital requirement by NBE the mean of the first three points lies between 3.41-4.2 with their respective standard deviations. The range where the mean is located implies that majority of the respondents have agreed with concepts raised. While the point “Providing longer period of time (5 years) to increase banks paid-up capital by NBE will not trigger merger and acquisition of banks” has a mean score of 2.1 with standard deviation 1.022. The range in which the mean exists indicates that majority of the respondents disagreed with the concept.

The descriptive statistics of the points under merger and acquisition decision have a mean score that is in the range 3.4-4.2 with their respective standard deviation depicted in the table above. The range in which the mean exists implies that majority of the respondents have agreed with the points raised under merger and acquisition decision.

Table 4. 10: Descriptive statistics of results on merger and acquisition decision

	Minimum	Maximum	Mean	Std. Deviation
Merger and acquisition decision of bank is undertaken in order to be secure from competitors and provide better services.	2	5	4.18	.841
Merger and acquisition decision of bank is undertaken to obtain synergy from banks' complementary skills and weaknesses.	2	5	4.02	.760
Banks decide to go for merger and acquisition in order to reduce various types of costs involved.	2	5	4.05	.819
Merger and acquisition decision is undertaken if banks want to increase capital with less hassle.	2	5	3.98	.808
Banks decide to go for merger and acquisition if banks want to diversify their services with less hassle.	2	5	4.12	.799

Source: SPSS output of the descriptive statistics on each of the Likert scale questions

4.3 Reliability Analysis

Reliability deals with the extent to which a measurement of a phenomenon provides stable and consistent result. It is also concerned with repeatability of results. Testing for the reliability is important as it refers to the consistency across the parts of a measuring instrument. A scale is said to have high internal consistency reliability if the items of a scale ‘hang together’ and measure the same construct (Taherdoost, 2018). The most commonly used internal consistency measure is the Cronbach’s Alpha Coefficient. When making use of Likert scale Cronbach’s Alpha Coefficient (α) is considered the most important measure of internal consistency. The most widely agreed internal consistency measure is an α value greater than 0.7.

Table 4. 11: Reliability analysis of the constructs

Construct	No of items	Alpha
Emphasis on increasing income	4	.765
Emphasis on decreasing operational cost	4	.818
Emphasis on increasing financial diversification	4	.769
Emphasis on market expansion	5	.785
Emphasis on maintaining capital requirement	4	.751
Merger and acquisition decision	5	.771
Over all of the constructs	26	.903

Source: SPSS output of reliability analysis

In this study reliability analysis is carried out on SPSS and the result of Alpha for each construct and the overall instrument is provided in table 11. From the table the Cronbach's reliability coefficient is greater than 0.70 for each construct and the overall Cronbach's Alpha is 0.903 which is an excellent estimate of reliability.

4.4 Correlation between variables

Correlation describes the strength of linear relationship between two random variables in terms of a single unitless value. Correlation takes values from -1 to +1. If $r = 0$, then there is no relationship between the two variables. If r is negative, there is an indirect relationship between the two variables. Whereas an r value of positive indicates that there is a direct relationship between the two variables.

Table 4. 12: Correlation between variables of the study

	EI	EC	EFD	EME	EMC	MA
EI	1					
EC	.639	1				
EFD	-.087	.028	1			
EME	.655	.674	-.101	1		
EMC	.642	.633	-.036	.677	1	
MA	.728	.763	-.042	.744	.747	1

Source: SPSS output of correlation analysis

The most widely used correlation measure is Pearson's correlation coefficient. It assumes that the two randomly distributed variables come from an interval data (Casson & Farmer, 2014). Pearson coefficient doesn't show relationship between variables. It indicates the strength of association between the two variables. The change in the magnitude of one variable is associated with a change in the magnitude of another variable in the same or opposite direction (Schober & Schwarte, 2018). A Pearson correlation is a measure of linear association between two normally distributed random variables. The correlation between variables of this study is provided in table 4.12.

4.5 Assumption of linear regression and diagnostics

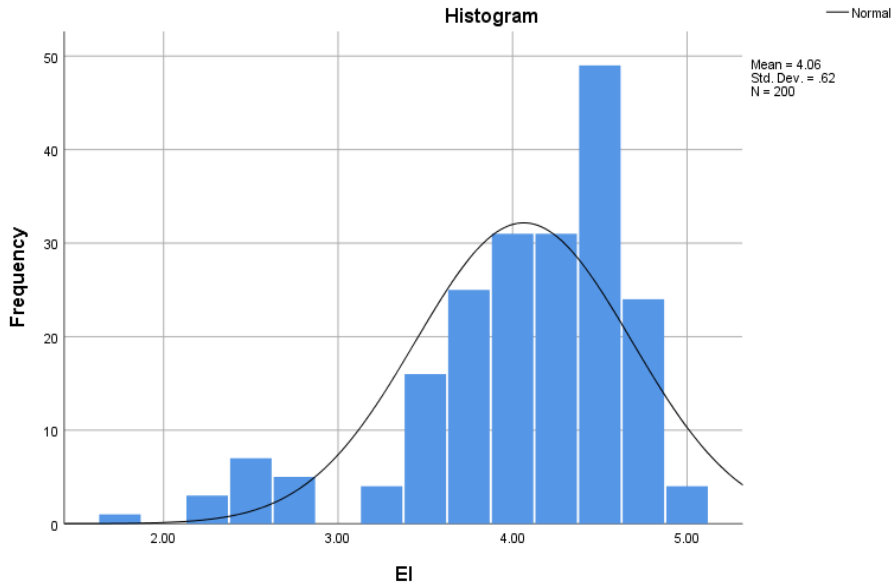
A statistical model is a simplification of reality expressed in mathematical language. When used appropriately, linear regression models a powerful statistical tool that can explain and predict real world phenomenon. However, misunderstanding of its assumption can lead to erroneous and misleading conclusion (Casson & Farmer, 2014). For a meaningful linear regression results there first assumption is assumptions regarding to the nature of the data set. The first assumption of classical linear regression model is normality of the data. A data set is normally distributed when the data has a bell-shaped symmetrical curve with zero mean and one standard deviation (Schreiber-Gregory & Bader, 2018). The second assumption is linearity which means that the dependent variable should be linearly correlated with the independent variables. For a CLRM the third assumption is that there should not be multicollinearity between the independent variables. Independent variables shouldn't have strong correlation among each other. The fourth assumption is assumption of homoscedasticity which means the variance of the residuals is the constant regardless of the dependent variable. The fifth assumption is there should be no

autocorrelation of the residuals. It means that the residuals should not correlate with each other. (Casson & Farmer, 2014; Schreiber-Gregory & Bader, 2018).

4.5.1 Normality test

Scholars over the years have debated over the existence of assumption of normal distribution from one extreme to another. Geary (1947) commented that normality is a myth, there never was and never will be normal distribution. Other scholars find out that if there is no normal distribution of data the associated normal and Chi-square tests are inaccurate and subsequently the t and F tests are not generally valid infinite sample. There are two types of normality test procedure. These are graphical method and analytical method. Graphical methods provide powerful diagnostic tools for confirming assumptions of normality. Histograms, stem and leaf plots, box plots, P-P plots, Q-Q plots have found the most application for normality testing. Histogram is a frequency distribution in which the observed values are plotted against their frequency, states a visual estimation whether the distribution is bell shaped or not (Rani Das, 2016).

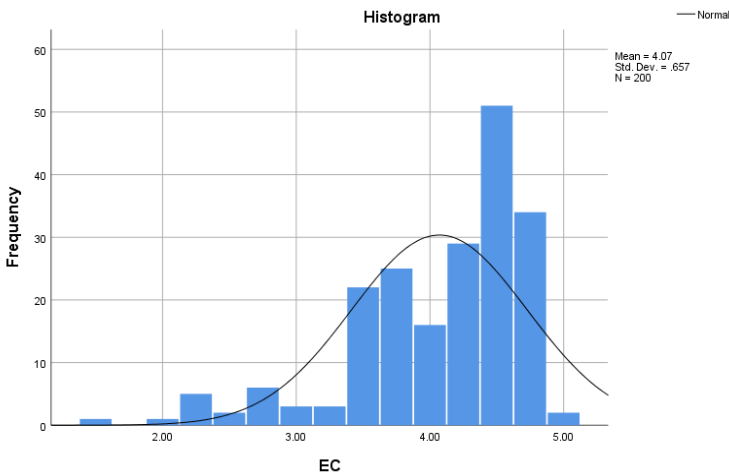
Non-normally distributed variables (highly skewed, kurtotic variables or variables with outliers) can distort relationships and significance tests. Normality of distribution of data set can be visually inspected by looking at P-P plots and histograms. Graphical approaches to explore model assumption are very helpful to fully understand one's data distribution (Astivia & Zumbo, 2019; Osborne & Waters, 2002).



Source: SPSS output of histogram plot of normality

Figure 4.1: Normality distribution of the data on emphasis on income

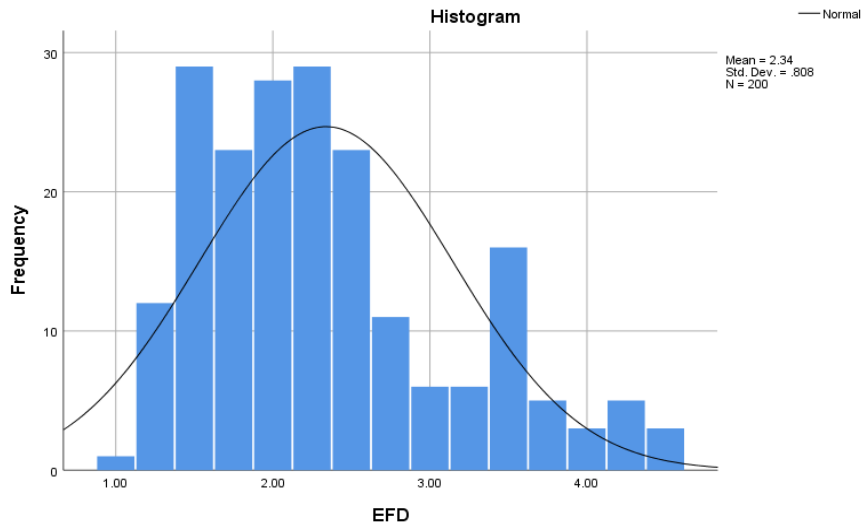
As it can be seen from the histogram of distribution of the data on EI, it almost follows a normal distribution curve, slightly skewed to the right.



Source: SPSS output of histogram plot of normality

Figure 4.2: Normality distribution of the data on emphasis on decreasing cost

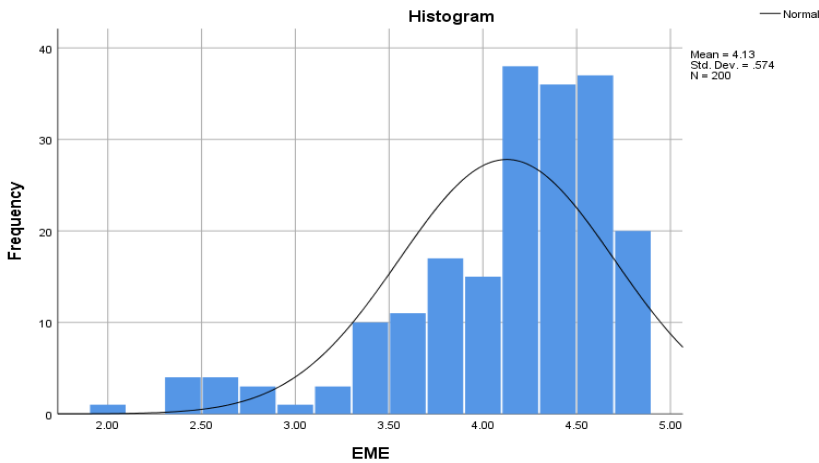
The figure shows that emphasis on decreasing cost approximately shows a normal distribution curve.



Source: SPSS output of histogram plot of normality

Figure 4.3: Normality distribution of the data on emphasis on financial diversification

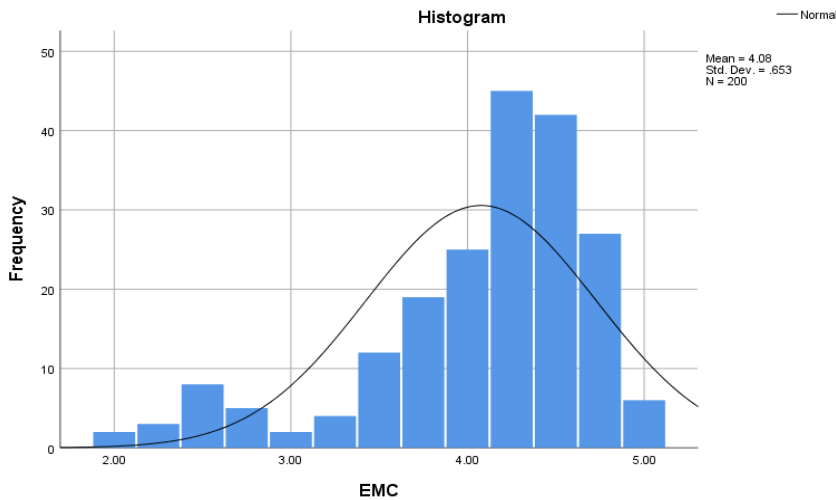
From the SPSS output of histogram diagram the financial diversification data set follows a normal distribution.



Source: SPSS output of histogram plot of normality

Figure 4 4: Normality distribution of the data on emphasis on market expansion

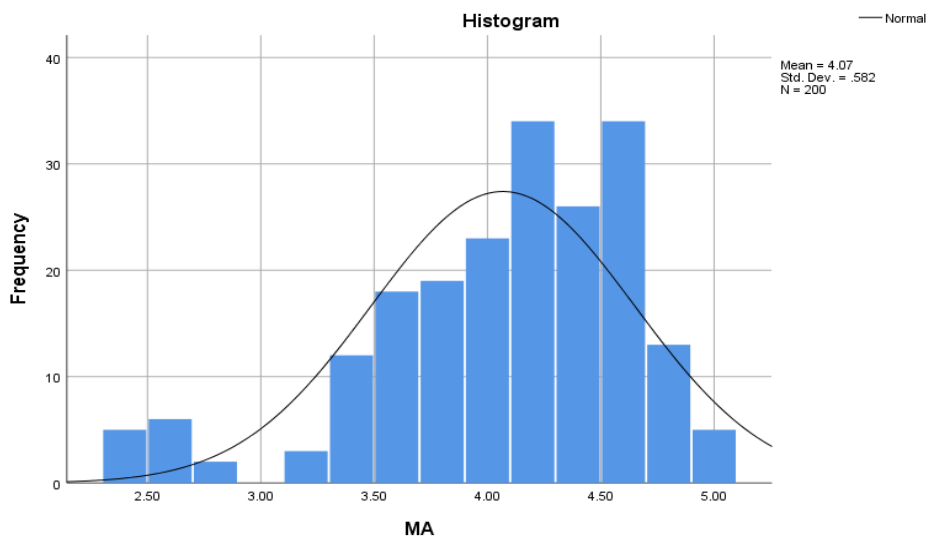
The graphical display of the market expansion data set approximately follows a normal distribution curve.



Source: SPSS output of histogram plot of normality

Figure 4.5: Normality distribution of the data on emphasis on maintaining capital requirement

The visual inspection of the histogram displays of maintaining capital requirement almost follows a normal distribution pattern



Source: SPSS output of histogram plot of normality

Figure 4. 6: Normality distribution of the data merger and acquisition decision

The dependent variable merger and acquisition histogram display shows a normal distribution curve of the data set. The visual display of the graphs of the scatter plot indicate that with a different level of skewness seems to follow normal distribution

However, the Kolmogorov-Smirnov statistical test shows that there is no normal distribution of the data

4.5.2 Test for no multicollinearity

CLRM takes the assumption that there should not be multicollinearity, strong correlation between the explanatory variables is unacceptable. This assumption is tested by looking at the correlation matrix of independent variables as well as by considering tolerance (T) and variance inflation factor (VIF). Tolerance measures the influence of one independent variable on all other independent variables. If tolerance (T) < 0.1 there is multicollinearity among the independent variables. The VIF is defined as $VIF = 1/T$. $VIF > 10$ indicates that there is multicollinearity (Schreiber-Gregory & Bader, 2018). Analysis of the VIF which is < 10 and $T > 0.1$ reveals that there is no multicollinearity among the independent variables.

Table 4. 13: Multicollinearity assumption test results

	Collinearity Statistics	
	Tolerance	VIF
EI	.459	2.180
EC	.444	2.254
EFD	.966	1.035
EME	.404	2.477
EMC	.448	2.233

Source: SPSS output of regression

4.5.3 Test for homoscedasticity

Linear regression assumes the presence of homoscedasticity. Homoscedasticity is the assumption that the residuals of the predicted variable should have a constant variance. It is an assumption that the residuals should be randomly distributed across the data set. Homoscedasticity means that the variance of errors is the same across all levels of the independent variables. The reverse of homoscedasticity is heteroscedasticity which is a situation where the condition of constant variance is violated. When the variance of errors differs at different values of the independent variables, heteroscedasticity is indicated. If a data set is heteroscedastic then the errors are dependent on the values of the independent variable and time series (Osborne & Waters, 2002). Heteroscedasticity can be induced either through the ways in which the dependent variable is measured or how the sets of the independent variables are measured.

Heteroscedasticity has little effect on significance tests. However, heteroscedasticity can lead to serious distortion of findings and seriously weakens the analysis. Heteroscedasticity doesn't bias the regression coefficient and the model fit but it does influence the uncertainty around it. Although the OLS regression coefficient of determination, R^2 , is not influenced the F-test associated with it is influenced. In addition, heteroscedasticity biases the standard error and test statistics (Astivia & Zumbo, 2019; Osborne & Waters, 2002).

The Breusch-Pagan test is one of the most common statistical tests of heteroscedasticity. It assesses where the model errors are associated with any of the model predictors.

H_0 = The variance of the error terms does not depend on the values of the independent variables (error variance is constant)

H_1 = The variance of the error terms depends on the values of the independent variable (error variance is not constant).

The rule of thumb for decision of Breusch-Pagan test is: If P value is less than $\alpha = 0.05$ reject the null hypothesis and conclude that there is heteroscedasticity. If P value is greater than $\alpha = 0.05$ then accept the null hypothesis that error variance is constant.

On SPSS the square of unstandardized residuals is regressed against all the independent variables.

Table 4. 14: ANOVA of the regression results of squares of unstandardized residuals on all independent variables

sModel		Sum of Squares	df	Mean Square	F	Sig.
	Regression	.023	5	.005	.292	.917 ^b
	Residual	3.017	194	.016		
	Total	3.039	199			

Source: SPSS output of regression result

The P value of the ANOVA of the regression of the squares of unstandardized residuals on all explanatory variables is 0.917, $P > 0.05$. This means that the null hypothesis is accepted. The variance is homoscedastic and there is no heteroscedasticity.

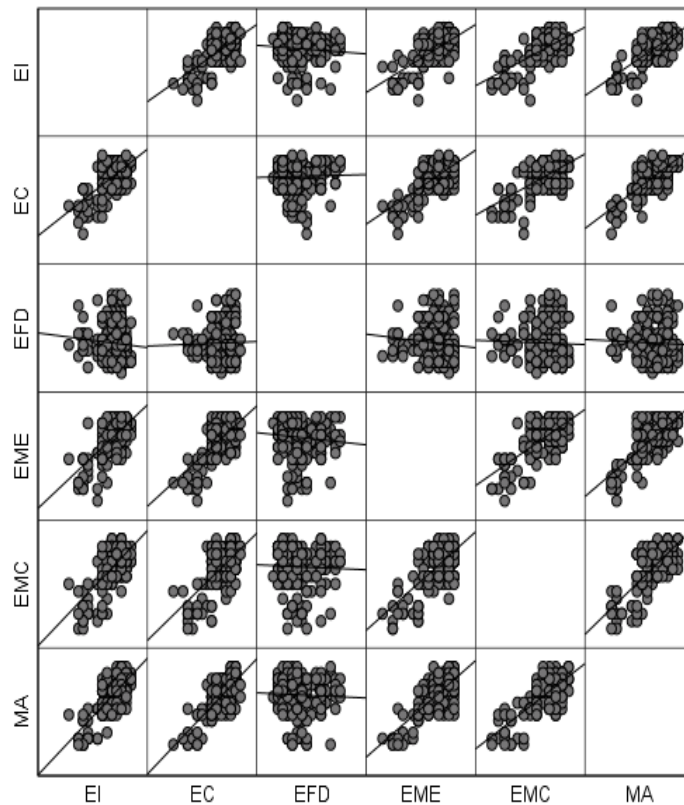
4.5.4 Test for absence of autocorrelation

Residuals should be independent from each other. Autocorrelation occurs when the residuals are not independent from each other. Autocorrelation can be tested by Durbin-Watson test. Durbin-Watson test D tests the null hypothesis that the residuals are not linearly autocorrelated. D can assume values between 0 and 4. The rule of thumb for the test values is $1.5 < D < 2.5$, shows that

there is no autocorrelation in the data (Schreiber-Gregory & Bader, 2018). In this study the Durbin-Watson value scores 1.85 which indicates that there is no autocorrelation in the data.

4.5.5 Test for linearity

The relationship between the dependent and independent variables should be linear. Constructing the scatterplot plot of the data is important in the data analysis. The plot should be approximately linear (Casson & Farmer, 2014).



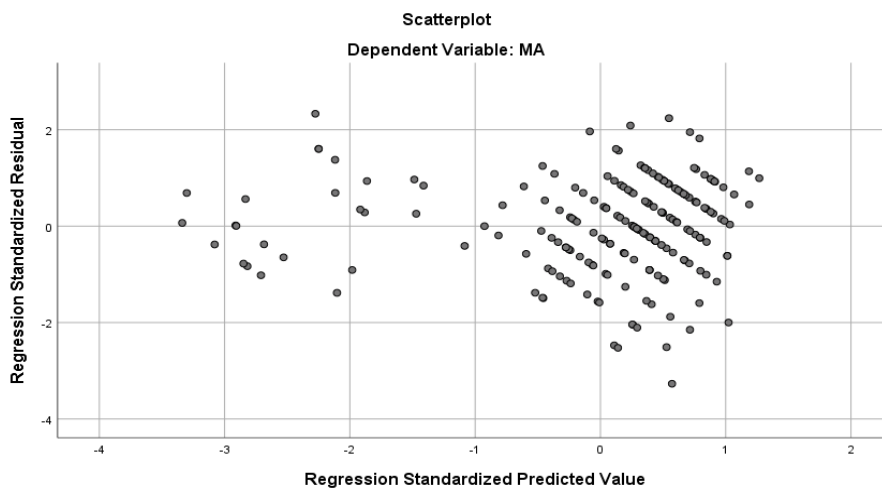
Source: SPSS output of the scatter plot of variables

Figure 4. 7: The scatter plot of variable

As it is depicted in figure 2 the scatter plot of the variables shows that there is a linear relationship between variables.

4.5.6 Test for normality of residuals and conditional zero mean of residuals

The residuals are assumed to have normal distribution with zero conditional mean and constant variance. Normality and zero conditional mean of the residuals can be assessed by looking at the scatter plot of residuals against the predicted values. Zero conditional mean can be detected by observing the scatter plot. Residuals should be scattered randomly around the zero line when standardized residuals are plotted against standardized predicted values. The scatter plot should be rectangular pattern with no values beyond -3 and 3 on both y and x axis.



Source: SPSS output of regression

Figure 4. 8: Scatter plot of standardized residuals against standardized predicted values.

From the scatter plot the residuals are distributed around the zero line. Some points are placed below -3. Generally, it seems that the residuals have zero conditional mean.

Normality of the residuals can be checked from statistical test of standardized residuals and predicted values.

The statistical tests of normality, both Kolmogorov-Smirnov and Shapiro-Wilk, are non-significant. The P value is > 0.05 , then we accept the null hypothesis that the distribution of the residuals follows a normal distribution pattern.

Table 4. 15: Statistical test results of normality of residuals

	Kolmogorov-Smirnov ^a			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
Unstandardized Residual	.045	200	.200*	.987	200	.055
Standardized Residual	.045	200	.200*	.987	200	.055

Source: SPSS output of normality test

4.6 Regression results

Regression techniques are possible for categorical and continuous variables. In linear regression the dependent variable should be in continuous measurement scale (Casson & Farmer, 2014). Linear regression is a method of data evaluation and modeling that establishes linear relationship between variables that are dependent and independent. Linear regression also can be used to determine causal relations between dependent and independent variables (Maulud & Abdulazeez, 2020). Parametric tests make assumptions about the underlying population from which the research data have been obtained, the population data are normally distributed. For an adequate sample size and normally distributed data parametric tests (t-test, ANOVA, Pearson correlation and regression) are used to analyze Likert scale data. Likert scale data are ordinal scale and non-parametric tests are suitable to analyze it. However, if the average of the ordinal data scale is computed then the ordinal average becomes a continuous scale and the use of parametric tests comes to be justifiable (Sullivan & Artino, 2013).

Dr Geoff Norman, one of the world's leader in medical education research methodology, asserted by using real and simulated parametric tests can not only be used with ordinal data, but

also parametric tests are more robust than non-parametric tests. Even if statistical assumptions of normal distribution of data are violated to an extreme degree, parametric tests tend to provide the “right answer” (Sullivan & Artino, 2013).

The data analysis procedures appropriate for interval scale items would include the Pearson’s, r, t-test, ANOVA and regression procedures.

This study is conducted to determine the factors that could trigger merger and acquisition of private commercial banks of Ethiopia. The explanatory variables that were proposed to impact MA are emphasis on income (EI), emphasis on cost (EC), emphasis on financial diversification (EFD), emphasis on market expansion (EME) and emphasis on maintaining capital requirement (EMC). Multiple linear regression is performed on SPSS by making MA dependent variable. The independent variable regressed are emphasis on income (EI), emphasis on cost (EC), emphasis on financial diversification (EFD), emphasis on market expansion (EME) and emphasis on maintaining capital requirement (EMC).

Table 4. 16: Regression result of ANOVA of the model

R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
				R Square Change	F Change	df1	df2	Sig. F Change
.868 ^a	.754	.747	.29269	.754	118.727	5	194	.000

Source: SPSS output of multiple linear regression of MA on all independent variables

The regression results of MA with all the explanatory variables revealed an R^2 value of 0.754. R^2 is a coefficient of determination which describes the proportion of the total variation in the dependent variable is explained by the dependent variables. It is the measure of the degree of agreement between the model and the outcome of the dependent variable. In other words, it is a

measure of how much we are reducing prediction error relative to how much potential error there is (Hagquist & Stenbeck, 1998). In this study, R^2 overestimates the goodness of fit of the model. For this reason, adjusted R squared is calculated to correct overestimation of the goodness of fit of the model. From the regression adjusted R squared = 0.747 which is slightly lower than R^2 . This is interpreted as 74.7% of the variation of the dependent variable is explained by the explanatory variables. The model significantly explains the variation of MA is explained by the explanatory variables at (F (5,194) =118.727), $P < 0.001$ by a percentage of 74.7. This can be observed from the ANOVA table of the regression model.

Table 4. 17: Regression output ANOVA of the model

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	50.856	5	10.171	118.727	.000 ^b
Residual	16.620	194	.086		
Total	67.475	199			

Source: SPSS output of analysis ANOVA

From the regression output of ANOVA, the sum of squares total (SST), sum of squares of errors (SSE) and sum of squares of regression (SSR) are obtained. The SST = 67.475, SSE = 16.620, and SSR = 50.856.

The regression output of the coefficients (β) of the regression model indicates that among the five variables hypothesized to trigger MA the explanatory variable emphasis on financial diversification is found not to significantly affect MA at a P value ($P = 0.981$).

The model that explains MA as dependent variable and the explanatory variables is provided as:

$$MA = .257 + .208 (EI) + .278 (EC) + .210 (EME) + .238 (EMC)$$

$$MA = 0.257 + 0.208 (\text{income}) + 0.278 (\text{Operational cost}) + 0.210 (\text{market expansion}) + 0.238 (\text{Capital requirement}).$$

All the explanatory variables positively affect MA. Emphasis on income ($\beta = .208$, $t = 4.202$, $p < 0.001$) triggers MA. This implies that the intention of banks to increase their income may lead to merger and acquisition with other banks. Emphasis on decreasing operational cost ($\beta = .278$, $t = 5.86$, $p < 0.001$) is indicated to necessitate MA. The explanatory variable Emphasis on financial diversification ($\beta = -0.001$, $t = -0.023$, $P = 0.981$) is found not to significantly affect MA activity.

Table 4. 18: Estimate of coefficients of the regression model

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
	B	Std. Error	Beta			Lower Bound	Upper Bound
(Constant)	.257	.178		1.450	.149	-.093	.608
EI	.208	.049	.221	4.202	.000	.110	.305
EC	.278	.047	.314	5.862	.000	.184	.371
EFD	-.001	.026	-.001	-.023	.981	-.052	.051
EME	.210	.057	.207	3.697	.000	.098	.323
EMC	.238	.047	.266	5.004	.000	.144	.331

Source: SPSS output of Coefficients of the regression

4.7 Hypothesis test results

The purpose of statistical inference is to draw conclusion about a population on the basis of data obtained from sample of the population. Hypothesis test is the process used to evaluate the strength of evidence from the sample and provides a framework for making determination about the population. The first step in testing hypothesis is the transformation of the research question into a null and alternate hypothesis (Davis & Mukamal, 2006).

Table 4. 19: Hypothesis test result

Hypotheses	Significance level	Status
<i>H1: Emphasis on product diversification leads to merger and acquisition of commercial banks.</i>	B = -.001, P = 0.981	Rejected
<i>H2: Higher amount of capital requirement than the previous by government regulatory body leads to merger and acquisition activity</i>	B = .238 P < 0.001	Accepted
<i>H3: The demand to raise income triggers merger and acquisition activity.</i>	B = .208 P < 0.001	Accepted
<i>H4: The need to minimize operational cost can trigger merger and acquisition of commercial banks</i>	B = .278 P < 0.001	Accepted
<i>H5: The desire to expand market share of commercial banks can lead to merger and acquisition activity.</i>	B = .210 P < 0.001	Accepted

The null hypothesis state that there is no association between the predictor and outcome variable in the population. The null hypothesis is the formal basis for testing statistical significance. The alternative hypothesis describes the existence of an association between the predictor and outcome and it is typically what the investigator wants to show. The alternative hypothesis cannot be tested directly. It is accepted by exclusion if the statistical significance rejects the null hypothesis (Banerjee et al., 2009; Davis & Mukamal, 2006)

The decision rule of rejecting null hypothesis:

If P value $P < \alpha$, then reject the null hypothesis and accept the alternative hypothesis.

If P value $P > \alpha$, then accept that the null hypothesis is true and reject the alternative hypothesis.

α is the predetermined statistical level of significance usually 0.05 and P value is the probability of obtaining the study results by chance if the null hypothesis is true.

4.8 Discussion

The study shows that emphasis on product diversification could not trigger merger and acquisition of private commercial banks in Ethiopia. A study conducted in the European Union has showed that gaining market power and diversification of revenues are the reasons for mergers (Figueiras et al., 2021). Increasing shareholders wealth is achieved by increasing market power and diversification as well reported by (Sarika & Vasantha, 2018). Study of banks in Kazakhstan showed that diversification of products is one of the factors that affect M&A (Smirnova, 2014). Diversification is the investment of different investments within a portfolio as a goal to reduce risk of portfolio. The reason for financial diversification not to affect merger and acquisition could be the less competition level of the banking sector. Extending services and products has an effect of increasing banking costs. If the cost of diversified products and services is not compensated by the income generated that will lead to reduction of income. The banks have not faced tougher competition so far and they are profitable. This could make them not to diversify their products as there is reduced risk of profitability.

Capital requirement by regulatory bodies is reported to affect MA. In this study the hypothesis *“Higher amount of capital requirement than the previous by government regulatory body leads to merger and acquisition activity”* is supported. Maintaining capital requirement stated by the NBE will trigger merger and acquisition waves in the future of private commercial banks. Factors that trigger merger and acquisition of banks can emanate from internal or external factors. Requirements set by regulatory bodies is one of the external factors that could lead to MA. Banking system of an emerging market is guided and directed by the regulatory bodies to maintain stability of the financial system. A study conducted in Lebanon showed that government deregulation policy led to the proliferation of private banks. Later, the government

declared a law that pushes banks to mergers and acquisition by making tighter capital requirements (Awdeh & EL-Moussawi, 2011). Even though merger among smaller banks is facilitated and motivated by regulatory authorities, merger among larger banks is not welcomed by regulatory authorities (Patty Duijm, 2018). Less capitalized banks are at high probability of being acquired. Government regulated MA is performed to reduce overcapacity and influences local banking system. Consolidation of banks in 1990 was performed by state authorities and the number of final number of banks were reduced from twenty-seven to seventeen (Mohamadi & Bohma, 2017).

The demand to raise income of banks is among the hypotheses tested in this study. The test showed that the intention of private commercial banks to increase income will lead merger and acquisition activities. The motive for any business entity is economic reason. In order to maximize shareholder value banks, undergo merger and acquisition. By doing so they increase financial efficiency and market power. Efficiency is improved when larger bank acquires smaller bank (Sarika & Vasantha, 2018). Most banks in the US and EU undergo consolidation for the sake of efficiency and stability. The consolidation of banks is facilitated by market forces (Figueiras et al., 2021). After studying 150 Slovenian companies (Lahovnik, 2016) showed that synergy of sharing activities, entering new market and financial synergy are the most common factors that affect MA.

Another hypothesis in this study is the demand to decrease operational cost will trigger merger and acquisition of private commercial banks. The study showed that the intention of private banks to decrease operational cost can lead to merger and acquisition decision. After studying a multiple of factors that affect M&A of banks in Nepal (Baniya & Shah, 2016) found that emphasis on cost efficiency, emphasis on providing service and better branding were the most

influential factors. In EU the most important driver of domestic consolidation is cost efficiency through economies of scale (Larsson & Wallenberg, 2002).

The last hypothesis of this study is that emphasis of banks to expand market share can trigger M&A is proved to significantly affect merger and acquisition decision. The fundamental aim of M&A is to adjust more efficiently to new opportunities and challenges. The main motive of bank M&A is to maximize shareholder value. This objective is achieved by increasing bank's market power and efficiency (Sarika & Vasantha, 2018). About 80% of M&A have multiple motives among these factors market timing synergy and response to economic or industry shocks are the most one (Nguyen et al., 2012). In developed countries market forces play a major role in M&A while in developing countries monetary authorities play a major role in bank M&A (Awdeh & EL-Moussawi, 2011). Thailand, Philippines and Malaysia have consolidated their banks slowly through the help of more of market forces. Market driven consolidation is relatively new type of banking consolidation in the last 20 years (Mohamadi & Bohma, 2017). Gaining market position and diversification are the main motives behind bank M&A in the EU (Figueiras et al., 2021). Study conducted in Nepal showed that market expansion cannot trigger M&A of banks (Baniya & Shah, 2016).

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1 Conclusion

Following the result of this study the following conclusion is made. As Ethiopia opens its banking system to foreign banks, domestic banks will experience a tough competition. This new competition will bring challenges and opportunities to the banking system. In order to cope up with the new challenge banks are expected to undergo merger and acquisition. The NBE Ethiopia has laid a tougher level of capital requirement for the establishment of new banks. This will make entry to the banking business difficult.

Emphasis on product diversification is not among the factors that could necessitate merger and acquisition. Obviously, the new government tighter capital requirement will induce merger and acquisition. Those banks which fail to meet the new bank establishment are likely to be merged or acquired. The desire of banks to increase income and to decrease operational cost can lead to merger and acquisition of private commercial banks. The need to market expansion is related with removal of rivals from the market. Market expansion emphasis is shown to necessitate merger and acquisition.

5.2 Recommendation

Merger and acquisition are almost a new phenomenon to the banking business of Ethiopia. In order to meet the new raised government capital requirement banks either have to collect additional capital or they are likely to undergo merger and acquisition. If banks do not want merge or not to be acquired, they need to issue new shares. Unless banks increase their income from their banking activities merger and acquisition is an option to increase income. If banks fail

to decrease their operational cost and as this will deplete income banks may be exposed to merger and acquisition. In order not to be acquired banks need to decrease operational cost. In order to survive in the business, banks need to capture a fair share of the market. As product diversification is not found not to significantly affect merger and acquisition the focus point of banks should not be on product diversification as it will lead to extra cost. This study is a preliminary in this new process. Further research should be conducted to find out whether other variables not identified in this study do affect merger and acquisition of private commercial banks and to make sufficient data for policy makers and business people.

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ANEX

Questionnaire used to collect data

Part I: General information

1. What is your gender?
 - a. Male _____
 - b. Female_____
2. What is your level of education?
 - a. BA degree
 - b. Master's degree
 - c. PhD
3. How many years of experience you have in the banking sector?
 - a. 5 – 10 years
 - b. 10 – 15 years
 - c. 15 – 20 years
 - d. > 20 years
4. What is your position in the bank you are currently working?
 - a. Bank manager
 - b. Senior banking officer
 - c. Member of board of directors (BOD)

Part II: Information on mergers and acquisition of private commercial banks operating in Ethiopia.

List of factors that could motivate merger and acquisition (M&A) of banks are provided in the following table. You are expected to provide your best level of agreement by marking (√) for each factor in the table. The value for each level of agreement is provided as; **5 = Strongly agree, 4 = agree, 3 = neutral, 2 = disagree, 1 = strongly disagree.**

S. No	Factors affecting merger and acquisition of private commercial banks in Ethiopia	Level of agreement				
		Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
	Emphasis on increasing income	5	4	3	2	1
1	Merger and acquisition may increase the net interest income of banks.					
2	Merger and acquisition may increase the non- interest income (income resulting from deposits, fees, service charges, e.t c.) of banks.					
3	The need to use multiple sources of income (like banking, microfinance) can be introduced with the help of merger and acquisition.					
4	Merger and acquisition help to increase the customer activity (opening new bank accounts, banking transaction, deposits etc).					
	Emphasis on cost efficiency					
5	Merger and acquisition help minimize the duplication of banking activities.					
6	Merger and acquisition eliminate branch overlapping.					
7	Banks under go merger and acquisition in order to reduce unnecessary managerial as well as operational positions.					
8	Providing more services using fixed set of premises can be obtained through merger and acquisition.					

	Emphasis on product diversification	5	4	3	2	1
9	Merger and acquisition are done in order to provide different types of products/services to customers					
10	Merger and acquisition are performed for the sake of managing financial complexities (example: managing non-performance of certain services)					
11	Merger and acquisition have role in creating portfolio of banks' products/services.					
12	In order to minimize market risk, merger and acquisition is performed by banks as a part of related diversification (activities that are similar to the one currently offered).					
	Emphasis on market expansion					
13	In order to obtain power and exclude rivals, banks go through merger and acquisition.					
14	Merger and acquisition have roles to capture market share.					
15	Merger and acquisition are effective tools for eliminating competition.					
16	Merger and acquisition make it easier for companies to obtain better market by increasing its size.					
17	In order to achieve success in key area of operations, merger is done with banks having deeper market penetration					
	Emphasis on maintaining capital requirement					
18	The new minimum paid-up capital requirement (5 billion ETB) to start banking business will trigger merger and acquisition					
19	Going for merger and acquisition is easier than issuing new shares for banks to achieve the new capital requirement					
20	Merger and acquisition help banks having trouble with minimum paid-up capital requirement					
21	Providing longer period of time (5 years) to increase banks paid-up capital by NBE will not trigger merger and acquisition of banks.					

	Merger and Acquisition Decision	5	4	3	2	1
22	Merger and acquisition decision of bank is undertaken in order to be secure from competitors and provide better services.					
23	Merger and acquisition decision of bank is undertaken to obtain synergy from banks' complementary skills and weaknesses.					
24	Banks decide to go for merger and acquisition in order to reduce various types of costs involved.					
25	Merger and acquisition decision is undertaken if banks want to increase capital with less hassle.					
26	Banks decide to go for merger and acquisition if they want to diversify their services with less hassle.					