Event Study of Effect of Merger Announcement on Stock Price in Nepal

Shanti Devi Chhetri¹, Ravindra Prasad Baral²

Abstract

Events like merger and acquisition affect the value of merging firms and also generate a positive or negative wealth effect for shareholders of firms involved. The purpose of this study is to investigate whether a merger announcement has generated wealth effects for the shareholders of bidding and target firms as well as it has aimed to assess the impact on overall banking sector. Two models: mean adjusted model and market risk adjusted model has been used in the study employing the ‘event study’ methodology to examine whether there is presence of abnormal return associated with merger announcement. In this method, 50 days premerger and 30 days post merger period is assumed as estimation period and (-15 and +15) days are taken as the window period. Fifteen financial institutions which entered into merger between years 2010 to 2012 are selected as sample. The findings of this study demonstrated that surrounding the announcement of merger proposals, the premerger abnormal return of individual firms is not significant to zero i.e. return is not affected by the merger announcement. Similarly, the abnormal return of bidding and target firms is not significant which indicates there is no impact of merger announcements on shareholder wealth in Nepalese capital market. Finally, the abnormal return during the premerger and post merger period of individual firms as well as the overall banking sector shows the same result, there is no significant difference on return before and after the merger announcement.

Keywords: Abnormal Stock Return, Capital Market, Merger and Acquisition, Signalling Effect

1. Introduction

Nepalese capital market is dominated by financial sector and is characterized by inefficient management, low volume of transactions, unhealthy competition, lack of competitive strength, lack of project financing, lack of skilled human resources, etc. Merger is an appropriate way to overcome these deficiencies. On other hand, Nepal government has opened the door for foreign banks and institutions after becoming the member of WTO. When there is good political and economic environment, no doubt; any time foreign banks would come up with high technical and capital resources. This situation will obviously create competitive pressures for domestic banks. Nepalese government has been offering various supportive policy levels to go for merger and Nepal Rastra Bank also been encouraging the bank and financial institution for institutionalising the merger and acquisition. Therefore, from strategic view point, the initiative of Nepal government the and NRB for proactive measures to safeguard the position of domestic banks should be appreciated.

Nevertheless, with increased liberalization and economic reforms in some countries in the region, more and more banks are getting merged for various reasons. The trend towards merger and acquisition has just started in Nepal from last decade. Laxmi bank merger with HISEF finance in 2004 is a significant milestone in the Nepali corporate sector. Later Nepal Bangladesh bank was merged with NB finance (within same group) in 2007. Likewise, H&B Development Bank came into existence after a merger between Himchuli Finance and Birgunj Finance. Kasthamandap Finance amalgamated with

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Banking reforms have allowed banks to engage in voluntary M&A which has led to high consolidating activity in the banking sector. The sample and methodology of this paper focused to see the relationship between merger announcement and stock returns.

The need for constant change in today’s dynamic business environment propels the companies to look for expansion by acquisition or merging with other companies (Shah & Arora, 2014). With the entry of new private banks, the domestic banks have been facing the pressure of competition. This is one reason why consolidation could be an imperative for Nepalese banks. Higher capital adequacy ratio of a bank indicates its potential for growth, financial solvency and ensures confidence for depositors. Capital deficient bank are unable to grow unless they augment the capital resources (Jayadev & Sensarma, 2007). The way out of this problem is to merge capital deficient bank with a bank of stronger capital base. In order to mitigate the risk of large capital inflows due to full convertibility of rupee on capital account, strong and large banks are needed and their evolvement is possible through consolidation.

Many banks are operating in urban areas, there is high competition on these areas and equally there is a regulatory pressure to expand services in rural part of the country. Banks that have already reached at rural areas and other which has to reach for business expansion; consolidation of banks through merger has been preferred choice for banks to grow and become big. From last few years, Nepalese banks have suffered from high liquidity crisis, many banks became problematic and some were closed down. To maintain the profitability and reduce competitive pressures, bank need to expand their services. Thus, through the merger and acquisition it has easier to go economies of scale for growth and profitability. Wong and Cheung (2009) indicates that corporate takeover is good news for the shareholders of bidding firms but not regarded as good news for the shareholders of the target firms. In addition, researchers confirm the hypothesis that the abnormal return for the shareholders of bidding firms during the post-announcement period depends on the type of acquisition. The existing empirical literature available on corporate restructuring events in Nepal and their effects on shareholders’ value is scanty; hence, there is a need for more studies on the subject. This study will help researchers to understand the concept of event study methodology and encourage analyzing the impact of corporate restructuring on stock returns. The main objective of this study is to assess the impact of merger announcement effect on share price and abnormal returns of financial institutions of Nepal during the pre and post merger announcement period. This study analyzes stock price behaviour before and after merger activity. It examines the abnormal return of each institution’s share price pre and post merger. It compares the impact of merger announcement on the acquirer and target firms’ stock price. The study focus on whether M&A in the Nepalese banking sector, spurred by the banking reforms, have actually improved bank performance for those banks involved. The stock price is related to only merger event. Specifically, the study adds to the merger literature related to signalling effect of merger announcement on value of the target and acquiring firm.

2. Literature Review

Khan and Ikram (2012) conducted the study with objective to test the efficiency of the Indian Stock Market with respect to the announcement of mergers and acquisition in the Indian Banking Sector by employing the standard Risk Adjusted Event Study Methodology. Their studies show the efficiency of the market in its semi strong form of EMH by accepting both the null hypothesis. It is observed that neither before nor after the merger announcement investors are able to earn abnormal/excess return. Padmavathy and Ashok (2012) investigated the informational value of merger announcement to the shareholders to earn abnormal return. The study concluded that a merger announcement does not hold important information to the Indian stock market during the study period. Return from the
announcement of merger and therefore the shareholders don’t reap any abnormal return.

Anand and Jagandeep (2008) have conducted the research on impact of merger announcements on shareholders. Wealth: Evidence from Indian private sector banks. This research report positive merger effects on the total wealth of shareholders in the private banking industry. Joshua (2011) attempted to make a comparative analysis of the impact of mergers and acquisitions on financial efficiency of selected banks in Nigeria. It was found that the post mergers and acquisitions’ period was more financially efficient than the pre-mergers and acquisitions period.

Bhardwaj (2014) studied with the objective to find out whether the merger and acquisition deal between the two banks ie (Centurion Bank and Bank of Punjab) was successful or not? The researcher concluded was that the merger activity has become good for both the banks, the overall efficiency and the productivity increases over the years. Sinha, Kaushik, and Chaudhary (2010) examined the impact of mergers and acquisitions on the financial efficiency of the selected financial institutions in India. The result of the study indicate that M&A cases in India show a significant correlation between financial performance and the M&A deal, in the long run, and the acquiring firms were able to generate value.

Gattoufi, Al-Muharrami, and Al-Kiyumi (2009) researched on the impact of mergers and acquisitions on the efficiency of GCC banks. The major result was that, though it was limited, there was a positive impact of M&A on the performance of commercial banks. Moreover, most of the banks involved in M&A realized an improvement higher than the average realized by the full sample, and hence improved their performances faster than the market. Mahmood, Aamir, Hussain, and Sohail (2012) studied the impact of merger/ acquisition on share price - A case study of Pakistan. The results indicate that M&A positively affect the share price of companies.

Sinha and Gupta (2011) studied mergers & acquisitions scenario of the Indian financial services sector. From the study it can be concluded that the M&A activity in the Indian financial services sector over a period of March 1993- Feb 2010 has had positive effects on the profitability in majority cases but the liquidity position has deteriorated in a period of three years after the merger. Liargovas and Repousis (2011) examined the impact of mergers and acquisitions on the performance of Greek banking sector. The overall results (the weighted average of gains to the bidder and target bank), indicated that bank mergers and acquisitions have no impact and do not create wealth.

3. Data and Methodology

3.1 Nature of Data and Sampling

This study is based on secondary data. The data for mergers and acquisitions is taken from the Nepal Stock Exchange; however, some of merged companies have been delisted by the NEPSE, thus, the Pre merger data of each firm were taken from merolagani.com. Based on the availability of data, following Bank and Financial Institution are selected as sample for the study:

<table>
<thead>
<tr>
<th>S.N</th>
<th>Pre Merger Name</th>
<th>Trading Halt Date At NEPSE</th>
<th>Post Merger Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Business Development Bank</td>
<td>29-09-2011</td>
<td>Business Universal Development Bank Ltd</td>
</tr>
<tr>
<td>2</td>
<td>Universal Finance Himchuli Bikash Bank</td>
<td>13-09-2011</td>
<td>H&amp;B Bank Ltd</td>
</tr>
<tr>
<td>3</td>
<td>Birgunj Finance</td>
<td>03-03-2011</td>
<td>MBL</td>
</tr>
<tr>
<td>4</td>
<td>Standard Finance Global bank ltd</td>
<td>11-12-2011</td>
<td>Global IME</td>
</tr>
<tr>
<td>5</td>
<td>IME</td>
<td>02-02-2012</td>
<td>Lord Buddha Finance</td>
</tr>
<tr>
<td></td>
<td>IME</td>
<td>02-02-2012</td>
<td>Kastamandap Development Bank Ltd</td>
</tr>
<tr>
<td>6</td>
<td>Shikhar Finance</td>
<td>NA</td>
<td></td>
</tr>
</tbody>
</table>

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All of the firms that have gone for merger in Nepalese history has been tried to bring under the study area. However, the companies that have already been delisted from the NEPSE made difficulty to get all price history for the study. Thus, on the basis of data availability, those banks and financial institution that have gone on merger process from January 1, 2010 to December 1, 2012 and have 30 days trading history after the merger completion are taken as a sample. Along with this we have assumed t=0 as an announcement period for the date at which individual bank’s trading has stopped or halted at NEPSE.

3.2 Event Study Method

Event studies method is arguably the best available instrument for measuring the impact of particular event on the phenomena. At any given point in time, security prices might be affected by a large number of randomly generated pieces of new information or events. Here the phenomenon is the shareholder return and merger is the event that could have impact on the shareholder perceptions and motives.

![Figure 1: Event Windows](image)

**Reason for Choosing the 15 Day Measurement**

The reason for choosing a 15 day measurement before and after the announcement is that the Nepalese capital market is not efficient even in weak form. Therefore, there is very few information as publicly available. And in case of merger in Nepal, merger practices are new. Merger proposal has to be passed from the general meetings but the partner is not defined. General meeting gives authority to board to conduct due diligence audit and choose the partner. The board conduct audit to find possible partner. From the day of audit they both request NEPSE to halt their share trade. In such case investor are informed only after the share halt. They play with the rumours till the official announcement of merger. Therefore, more the event period is taken, more the shareholder or investor are informed and confirmed about the events. In such conditions, 15 day measurement before the announcement is important in order to detect any price movement as a result of any rumours of merger proposals.

3.3 The Market Model

In this method, value of α and β are calculated from the estimation period. After this, forecast of the return of individual security can be done. \( e_t \) is the estimation of residual value from which we calculate the abnormal return of a security. Share price performance from the event \( t=-50 \) to \( t=-15 \) to \( t=15 \) to \( t=30 \) days is used to estimate the parameters of the market model, and the abnormal rate of return of the merging firms during the window period (pre and Post announcement period) is estimate using the parameter. The abnormal return captured by residual’s of firm \( i \) on day \( t \) is expressed as

\[
e_t = \alpha + \beta R_{mt} \quad \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots (1)
\]

Where:

- \( R_t \) = daily share return for firm / in day \( t \)
- \( \alpha \) = the intercept term
- \( \beta \) = the systematic risk of share
- \( R_{mt} \) = rate of return on a market index in day \( t \) relative to the announcement of offer
- \( e_t \) = residual term
- \( t = -15 \ldots +15 \) days

The daily share return, \( R_t \) can be calculated from the formula:

\[
R_t = \frac{(P_t - P_{t-1})}{P_{t-1}} \quad \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots (2)
\]

Where:

- \( P_t \) = price per share of common stock of firm / at the end of day \( t \)
- \( P_{t-1} \) = price per share of common stock of firm / at the end of day \( t-1 \)

Market Return, \( R_{mt} \). Can be calculated from the formula

\[
R_{mt} = (M_t - M_{t-1})M_{t-1} \quad \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots (3)
\]

Where:

- \( t = -15 \ldots , +15 \) days
The abnormal returns for firm I in day $t$, $AR_{dit}$, based on the market model can be defined as:

$$AR_{i} = R_{i} - \alpha - \beta R_{m} \quad \ldots \ldots \ldots \quad (4)$$

or

$$AR_{i} = R_{i} - e_{i} \quad \ldots \ldots \ldots \quad (4)$$

where $e_{i}$ and $R_{i}$ for individual firm are calculated daily by using the equation (1) and (2) from the event $t=-15$ to $t=15$ days.

The cumulative abnormal return, $CAR_{i}$, for the bidders and the target firms for the period of $t = -15$ to $t = 15$ can be defined as:

$$CAR_{i} = \sum_{N_{t-1}}^{N_{t}} AR \quad \ldots \ldots \ldots \quad (5)$$

### 3.4 The Mean adjusted model

The Mean adjusted model is practically simpler than the market model; it is widely used as a comparison for the market model for some research on event studies. In this model we assumed that the normal return for the security equals a constant $K_{i}$ (Mean Value) over the estimation period. The expected return for the security is assumed to be constant over time, though ex-ante return will vary among securities. Thus, abnormal return for the security is found:

$$AR_{i} = R_{i} - K_{i} \quad \ldots \ldots \ldots \quad (6)$$

Where,

- $R_{i}$ = day of return on day $t$
- $K_{i}$ = Mean value of the daily return

Daily return can be calculated as:

$$R_{i} = \frac{(P_{1} - P_{0})}{P_{0}} \quad \ldots \ldots \ldots \quad (7)$$

Where,

- $P_{1}$ = price per share of common stock of firm / at the end of day $t$
- $P_{0}$ = price per share of common stock of firm / at the end of day $t-1$
- $t = -15 \ldots +15$ days

The cumulative abnormal return, $CAR_{i}$, for the bidders and the target firms for the period of $t = -15$ to $t = 15$ can be defined as:

$$CAR_{i} = \sum_{N_{t}}^{N_{t-1}} AR \quad \ldots \ldots \ldots \quad (8)$$

### 3.5 Hypotheses Development

The study attempts to analyze whether merger announcement made by both bidder and target companies have significant impact on the company’s stock returns. Different t-tests (one sample t-test, independent sample t-test) is used to test the hypothesis presented below. To test for the significance for individual firms, one sample t-test has been conducted in which we have set the following hypothesis assumption:

$H_{1}$: Merger announcement have a significant impact on stock returns.

$H_{1}$: $AR \neq 0$

To test the difference in mean abnormal return between target and acquiring firm; Pre and Post merger impact, the Independent Sample T-test has been conducted for testing equality of mean returns.

$H_{2}$: Merger announcement have significant impact on stock returns between the firms or Pre merger return and Post merger return.

$H_{2}$: $AR_{Firm(A)} \neq AR_{Firm(B)} \quad OR \quad AR_{(Pre)} \neq AR_{(Post)}$

### 4. Empirical Analysis

The Table II exhibits the abnormal return and cumulative abnormal returns calculated using the market adjusted model and mean adjusted model. The values are calculated for the event window period of 15 days. The t-test result is also presented to test if the abnormal returns are significantly different from zero. It is expected that if the positive signalling effect from merger announcement is present than the abnormal stock returns during the period will be positive.

Table II reveals that the average abnormal return (AR) of overall firms from both mean adjusted and Market adjusted models. There is positive return of 0.02501 and 0.02855 after the merger announcement from both models. While we compare the return from both model, we can found highest return from mean model on day

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(t=4) of 0.03089 and lowest return on day (t=-10) is -0.03281. Both the model shows the positive returns from announcement period to day (t=4).

Table II: Market Adjusted Model and Mean Adjusted Model

<table>
<thead>
<tr>
<th>Days</th>
<th>Mean Adjusted</th>
<th>CAR Market Adjusted</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>0.02501</td>
<td>0.02855</td>
</tr>
<tr>
<td>2</td>
<td>0.01400</td>
<td>0.02907</td>
</tr>
<tr>
<td>3</td>
<td>0.02453</td>
<td>0.02000</td>
</tr>
<tr>
<td>4</td>
<td>0.03089</td>
<td>0.02250</td>
</tr>
<tr>
<td>5</td>
<td>-0.02696</td>
<td>-0.02976</td>
</tr>
<tr>
<td>6</td>
<td>-0.00715</td>
<td>-0.00860</td>
</tr>
<tr>
<td>7</td>
<td>0.00322</td>
<td>0.00278</td>
</tr>
<tr>
<td>8</td>
<td>-0.01358</td>
<td>-0.01533</td>
</tr>
<tr>
<td>9</td>
<td>-0.01558</td>
<td>-0.01045</td>
</tr>
<tr>
<td>10</td>
<td>-0.03281</td>
<td>-0.02732</td>
</tr>
<tr>
<td>11</td>
<td>-0.01864</td>
<td>-0.01057</td>
</tr>
<tr>
<td>12</td>
<td>-0.00812</td>
<td>-0.00164</td>
</tr>
<tr>
<td>13</td>
<td>0.01030</td>
<td>0.00439</td>
</tr>
<tr>
<td>14</td>
<td>-0.00062</td>
<td>-0.00028</td>
</tr>
<tr>
<td>15</td>
<td>-0.00321</td>
<td>-0.00596</td>
</tr>
</tbody>
</table>

t value | -.251 | -.478
Std error | 0.0496 | 0.00431
sig. | .805 | .640

Here the calculated t – statistic of both mean adjusted and market adjusted return models is -.805 and -.640 simultaneously. The test shows that the abnormal returns before the merger announcement are not significant. Hence the null hypothesis accepted that means abnormal return of sampled banks is zero. It suggests that the pre merger information doesn’t have significant influence in increasing the stock price.

Table III presents the results of independent samples t-test which examines the equality of the pre and post merger abnormal return. The results reveal that the pre-merger abnormal return (AR) of the individual banks under Market adjusted model is not significantly different than their post-merger abnormal return except in the case of Birgunj Finance. Hence, the null hypothesis is accepted in most of the cases which means the abnormal return of sampled banks is zero. The findings suggest that the merger announcement doesn’t have much effect on the stock returns of both the target and bidder firms. As the abnormal returns are found to be similar in both the pre and post merger period, the signalling effect of the merger announcement is found to be absent. The results seem to suggest that mergers don’t create value for the shareholders.

Table III: Pre and Post Merger Abnormal Return Analysis between Merging Partner (Market Adjusted Model)

<table>
<thead>
<tr>
<th>Firm</th>
<th>Null Hypothesis</th>
<th>Premerger AR</th>
<th>Post merger AR</th>
<th>t-statistics</th>
<th>Df</th>
<th>Sig</th>
<th>AR_{pre} = AR_{post}</th>
</tr>
</thead>
<tbody>
<tr>
<td>BDBL</td>
<td>Accept</td>
<td>0.88</td>
<td>16.227</td>
<td>0.931</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>UF</td>
<td>Accept</td>
<td>.700</td>
<td>28</td>
<td>.489</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Birgunj</td>
<td>Reject</td>
<td>-1.705</td>
<td>28</td>
<td>0.099</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MBL</td>
<td>Accept</td>
<td>.903</td>
<td>20.258</td>
<td>.377</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Standard</td>
<td>Accept</td>
<td>-.137</td>
<td>28</td>
<td>.892</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global</td>
<td>Accept</td>
<td>-.864</td>
<td>14.265</td>
<td>.402</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ime</td>
<td>Accept</td>
<td>1.080</td>
<td>28</td>
<td>.289</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lord Buddha</td>
<td>Accept</td>
<td>1.496</td>
<td>28</td>
<td>.146</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kastamandav</td>
<td>Accept</td>
<td>-.863</td>
<td>28</td>
<td>.395</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Null hypothesis AR_{pre} = AR_{post}: Premerger AR is equal to Post merger AR
4.2.2 Mean Adjusted Model

Table IV: Pre and Post merger Abnormal Return Analysis between Merging Partners (Mean Adjusted Model)

<table>
<thead>
<tr>
<th>Firm</th>
<th>Premerger</th>
<th>Post merger</th>
<th>t-statistics</th>
<th>Df</th>
<th>Sig</th>
<th>AR$<em>{pre}$ = AR$</em>{post}$</th>
</tr>
</thead>
<tbody>
<tr>
<td>BDBL</td>
<td>.365</td>
<td>.16.889</td>
<td>.720</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UF</td>
<td>.678</td>
<td>.28</td>
<td>.505</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Himchuli</td>
<td>.678</td>
<td>.28</td>
<td>.505</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Birgunj</td>
<td>.893</td>
<td>.19.659</td>
<td>.335</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Standard</td>
<td>.216</td>
<td>.21.425</td>
<td>.831</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global</td>
<td>1.025</td>
<td>.18.86</td>
<td>.318</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>IME</td>
<td>.893</td>
<td>.28</td>
<td>.379</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lord Buddha</td>
<td>.660</td>
<td>.22.671</td>
<td>.516</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kastamandav</td>
<td>-.528</td>
<td>.28</td>
<td>.601</td>
<td>Accept</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Null hypothesis $AR_{pre} = AR_{post}$: Premerger AR is equal to Post merger AR

Table IV reveals that the abnormal return (AR) of premerger individual bank and in respect to their post merger banks under Mean adjusted models. The test shows that the abnormal returns between premerger and Post merger returns are not significant. Hence the null hypothesis accepted that means abnormal return of sampled banks is zero. It suggests that the merger information doesn’t have significant influence in increasing the stock price.

4.3 Pre and Post Merger Abnormal Return of Overall Banking Sector

4.3.1 Mean Adjusted Model

Table V: Pre and Post Merger Abnormal Return of Overall Banking Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>t-statistics</th>
<th>Df</th>
<th>Sig</th>
<th>AR$<em>{pre}$ = AR$</em>{post}$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean model</td>
<td>.025</td>
<td>19.118</td>
<td>.980</td>
<td>Accept</td>
</tr>
</tbody>
</table>

Note: Null hypothesis $AR_{pre} = AR_{post}$: Premerger AR is equal to Post merger AR

Table V reveals that the Pre and Post abnormal return (AR) of overall banking sector under the mean adjusted model analysis. The test shows that the abnormal returns between premerger and Post merger returns are not significant with the assumption of Null hypothesis $AR_{pre} = AR_{post}$: Premerger AR is equal to Post merger AR. Hence, the results seem to offer some preliminary evidence that the efficiency of the market of Nepal falls under semi strong forms EMH by accepting null hypothesis because neither before nor after the merger announcement investors are able to earn abnormal return. However, the issue requires further investigation.

4.3.2 Market Adjusted Model

Table VI: Pre and Post Merger Abnormal Return of Overall Banking Sector

<table>
<thead>
<tr>
<th>Model</th>
<th>t-statistics</th>
<th>df</th>
<th>Sig</th>
<th>AR$<em>{pre}$ = AR$</em>{post}$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market</td>
<td>-.202</td>
<td>19.789</td>
<td>.842</td>
<td>Accept</td>
</tr>
</tbody>
</table>

Note: Null hypothesis $AR_{pre} = AR_{post}$: Premerger AR is equal to Post merger AR

Table VI reveals that the Pre and Post abnormal return (AR) of overall banking sector under the market adjusted model analysis. The test shows that the abnormal returns between premerger and Post merger returns are not significant with the assumption of Null hypothesis $AR_{pre} = AR_{post}$: Premerger AR is equal to Post merger AR. Hence, it is evidenced that the efficiency of the market of Nepal falls under semi strong forms EMH by accepting null hypothesis, cause neither before nor after the merger announcement investors are able to earn abnormal return.

From the figure II it can be analyzed that abnormal return prior to merger announcement is less volatile with respect to post merger announcements. One day after the announcement (t=1), the share price decreases but after that the share price trend is to increase gradually. This can be interpreted as the shareholders and investors believing...
that merger proposals will generate some advantages. This situation also create optimism in shareholders and investors that the merger proposal will drive up the value of their shares which in tum will maximise their wealth effect.

Certain empirical evidence indicates substantial excess returns to the stockholders of the target company after the merger announcement. This wealth increment is due to the premium paid by the acquiring company for the target and synergistic benefits expected to occur due to merger. Typically, the stock price improvement begins prior to the merger announcement. However, for the acquiring company stockholders, the evidence is mixed. For acquiring company the premium paid for the target and its justification in terms of expected synergy and more efficient management of the resources of the target company determines the abnormal returns. This study reveals that the abnormal returns due to merger announcements are not significant and the pre and post merger abnormal returns are not significantly different. The results reveal that merger announcement in Nepal don’t create value for both the merging firms. The positive signalling effect of merger announcement is absent. The theoretical justification of the result is that the stock market of Nepal is not efficient even in weak form. Hence, the information on merger announcement is not fully reflected in share prices of the target and bidding company.

5. Conclusion

From market adjusted model, the abnormal return of global bank is higher than the other firms where as IME have lowest and negative abnormal returns. According to the mean adjusted model, IME has the highest abnormal return among the merging companies. However, the assumption of merger impacts on shareholder’s return (AR=0) has been proved caused none of the firms is significant on the basis of analysis. Since the abnormal return of individual bank has been proved as an insignificant, between the merging partner and the abnormal return between the bidder and target firms also found as there is no significance difference on shareholder’s return due to the merger announcement. Here in context to Nepal, the investor’s motive has not changed on the merging firm’s size, growth and profitability either investor are less informed about the market events. This result has proved that, an involuntary merger activity has not able to grab the attention of investors. Similarly, the Mean adjusted model analysis of abnormal returns between the firm’s pre merger announcement and post merge announcement also, the results are proved according to our assumption i.e. none of the firm’s pre merger abnormal returns different in respect to their post merger firms. While according to the market adjusted model, pre merger Birgunj finance’s abnormal return is different in respect to its post merger firms i.e. H&B. Except the Birgunj and H&B, other firm’s abnormal return between pre and post merger are equal. The entire firm’s test statistics depicts that the null hypothesis is accepted in an assumption of pre merger abnormal return of firms is equal to the post merger abnormal return. The test statistics is insignificant in all cases of selected firms, so it clear that the announcement of merger news has not made impacts on the investor’s perceptions and motives. While talking the merger impacts on overall banking system, from aspects of both Mean and Market adjusted model also the entire firm’s test statistics depicts that the null hypothesis is accepted in an assumption of pre merger abnormal return of firms is equal to the post merger abnormal return. The test statistics is insignificant in all cases of overall banking sector, so it clear that the announcement of merger news has not made impacts on the investor’s perceptions and motives. For strengthen the banking sector, NRB is using the various policies and directives. Involuntary merger concept is not working; the investors and bankers are not willing in favour of merger policies in such conditions the impact is less effective. And another reality of no impacts on shareholder is, inappropriate partners. Partners should be chosen from same category. Same class partnership could create great impacts on shareholder’s returns. Banks are just fulfilling the compliances of NBB’s Directives not for gaining the advantages of synergy impacts. This study was conducted with the aim to find the market
efficiencies, the evidence here supports the efficiency of the market in its semi strong form of EMH by accepting both pre and post merger null hypothesis. It is observed that neither before nor after the merger announcement investors are able to earn abnormal/ excess return. Similarly the hubris theory assumptions are not found in Nepalese capital market. Random abnormal returns are found in between the return of bidder and target. At the end it is concluded that the merger practices do not have positive impact on shareholders return. Pre merger abnormal return is not significant with the post merger abnormal return. Neither before nor after the merger announcement, were investors able to earn abnormal return. From the study it can be inferred that in context of Nepal, a merger activity is unable to create positive impacts on shareholder perception and motives.

This study is significant not only to the shareholders who are an important stakeholder of a banking firm but also to policy makers because in a country like Nepal where public sector banks dominate the banking industry, it is the Government who is the major owner of such enterprises and will incur financial loss if mergers are not creating any wealth. Most of the bank mergers in Nepal are policy driven and not market driven, hence it is important for the policy makers to understand that their policies have added value for all the stakeholders or not.

References


Event Study of Effect of Merger Announcement on Stock Price in Nepal


