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Mergers and Acquisitions in the Banking Industry: Britain 1885-1920

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Abstract

Mergers and acquisitions among banks remain an understudied area of finance. Most of the analyses have used small sample sizes over a relatively short period of time where governments and anti-trust authorities can regulate M&As activities among financial companies. No study has disentangled the wealth effects of publicly versus privately held target banks.

We address these issues by studying wealth effects for banks during the forty year wave of mergers and acquisitions in the United Kingdom between 1885 and 1925. During this period, the country's banking sector became much more concentrated. Anti-trust authorities and legislation did not exist in the period; mergers, even between large banks were possible and did occur especially in the first two decades of the twentieth century. The analysis of this historical period allows us to study mergers and banks takeovers over a very long period of time. We examine how wealth effects of M&A deals changed while the banking industry was becoming more and more concentrated. Our data also allow to compute wealth effects distinguishing between deals involving publicly held targets versus privately held targets. While this issue has been studied in corporate finance for non-financial firms (Chang (1998) and Faccio, McCollen and Stolin (2006)), to the best of our knowledge, such an analysis has not been undertaken for the banking industry.

In a sample that consists of more than eighty takeovers, we find positive wealth effects for bidders in the order of 1.5% during the month of the M&A announcement. This result

is different from most of the studies that utilize recent years' data that found zero or negative wealth effects for bidders. Also targets experienced positive returns of about 7%. When we split our sample in two sub-periods, 1885-1905 and 1905-1925, we find that wealth effects for bidders are positive and equal to 1.7% in 1885-1905 whereas, although remaining positive at 0.8% in 1906-1925, they are no longer statistically significant; wealth effects are higher for targets in the second period. In contrast to corporate finance analysis we find that the bidder displayed positive wealth effects when it took over a joint stock publicly traded bank, whereas returns were negative and not statistically significant when the bidder acquired a private bank. Small private banks, their owner-partners and their managers, were believed to invest to a large extent into the acquisition of information about borrowers. Most of this information was "soft": not easily transmittable from person to person and it could only slowly be acquired through time. In many cases the old partners or managers of the private target banks were replaced by new officers who did not have the same specific knowledge about customers. As a result the information acquired by the previous managers was lost. Our findings are consistent with a hypothesis that the market priced the depletion of information caused by the acquisition.