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BANKING CONSOLIDATION AS VALUE CREATION TO THE BUYER AND THE FINANCIAL SYSTEM (CASE OF LITHUANIA)

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Abstract. The banking and finance sector is one of the most dynamic sectors that is continuously experiencing most of structural changes. Fast consolidation and concentration of banks globally has evoked active discussions on behalf of scientists and practitioners on the effect gained from concentrating on the efficiency and competitiveness of the banking system, financial and microeconomic stability of countries and economic development. Mergers and acquisitions of the banking sector are mostly encouraged by the target to get more authority in the international banking environment, to eliminate competitors from profitable activity and to strive for additional financial benefit for shareholders, to increase the range of the services provided, to use the resources efficiently, i. e. to create the value for shareholders and to contribute to the development of the financial sector. Therefore, the article analyses the bank mergers and acquisitions of the Lithuanian banking sector; it is assessed whether the bank mergers have created the value for shareholders and (or) the financial system. The research that has been carried out shows that mergers and acquisitions of the banking sector are take placing in order to increase the benefit for shareholders and to strive for the economy; the aspect of financial stability of such transactions appears in a short term and is most commonly inspired by the government. Modern Lithuanian banking sector has been formed by means of mergers and acquisitions; strategic investors helped transitive economy countries to guarantee the stability of the banking sector and to achieve the benefit of the economy of scale. Restructuring of the banking activities, i. e. the performance distribution can be a useful measure in ensuring stable activities of both the financial system and the accepting bank – to acquire a market share and to optimise its performance.

Keywords: banking, financial intermediaries, regulation, value creation, mergers, acquisitions, restructuring, market structure

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1. Introduction

In the historical retrospective of the last decades there have been several cases when banks acquired other banks thus getting new opportunities to develop their activity. Acquiring the competitors, banks reduced market competition, increased their market share, reduced service provision expenditure using the effect of the economy of scale. In addition, more liberal regulation of financial institutions at the end of the 20th century and the beginning of the 21st century provided the opportunities for banks to merge with different providers of financial services and thus take advantage of the economy of scale, when the institutions providing various financial services (e. g. provision of loans, insurance, financing trade, investment management, etc.) belong to one financial institution – financial aggregation. The institution thus becomes less dependent on its clients, on the reduction of one provided service and becomes a more diversified service provider. This situation can also be explained by the Markowitz Portfolio Theory, when portfolio diversification disperses (reduces) the risk. However, there are certain barriers for financial services sector (banks, insurance companies, etc.) to enter the market (capital requirements, activity risk limitations and other), thus it can be stated that only a limited number of participants can provide services on this market.

The activity of modern banking sector is multilateral and miscellaneous, especially of the banks forming or being part of financial groups or aggregates. Multilateralism and current activity of banks can be regarded to be a great challenge for the banking sector. The authors opinion is that modern financial world, especially the competition between the members of the financial sector, fast development, the application of modern technologies in the activity, the changes in the regulation and supervision of the financial system, the recent global financial crisis has a very strong effect on the financial sector. Currently, the improvement of the banking sector supervision and regulation has an exceptional effect on it.

It should be noticed that the problem of mergers and acquisitions has been widely analysed and there are special literature theories explaining the motives of this process. Harford (2011), concluding the motives of mergers and acquisitions, states the motives and the reasons explaining these processes which can be ascribed to neoclassical, agents and behavioural theories. Piesse *et al.* (2013), analysing the motives of mergers and acquisitions, distinguish 8 theories (hypotheses), which explain the process of mergers and acquisitions on the market. Novickytė, Saikevičius (2013) show that separate hypotheses in the literature sometimes intertwine, and thus ascribe them to the main theories distinguished by Harford (2011).

Different authors and research (Berger *et al.* 2000; European Central Bank 1999; Grundey 2008) show that bank consolidation in Europe and the world was mainly determined by the increased performance efficiency, when there were attempts to merge several banks or other financial institutions into one which, due to its size, could provide its services cheaper and, what is more, optimise the representation network of a branch of the bank or any other financial institution. Heffernan (2005) divides the reasons of bank mergers into three categories: maximising shreholder's equity/return, striving for self-interest of bank managers and other reasons (increased competition of the members of non-bank services; bank services' development, increasing banks' non-balance indicators; innovations and IT development in the banking sector, which help to strive for the optimisation of activity expenditures, increasing income and generaiting additional income from bank services using financial innovations), which create a positive environment for mergers and acquisitions.

Authors (Dermine 1999, 2002; Hernando *et al.* 2009) state that there are other reasons which encourage mergers and acquisitions in the banking sector. In general such transactions are determined by the improvement of the purchased company's shareholders benefit. Still 10 main reasons are distinguished while determining mergers and acquisitions in the banking sector: the economy of scale based on expenditure, the economy of scale based on the trademark, the economy of scale based on income, the economy of scale based on security, the economy of expenditure, the economy, based on selling, the economy based on financial diversification, X efficiency, market power, the economy of scale based on defence.

Authors (Bottiglia *et al.* 2010), analysing the motives of banks and other financial sector's members' mergers, divide them into endogenous (increasing the activity of the market, the economy of scale, the optimisation of management structure, the opportunity to avoid opposite takeover, increasing shareholder's return, settling bank management and status) and international (the development of bank activity). Asimakopoulos and Athanasoglou (2013), Caruso and Palmucci (2011), Altunbas and Ibáñez (2004), Beitel and Schiereck (2001) having analysed the creation of value in the banking sector through mergers and takeover, have established that bank target shareholders receive greater abnormal return than the owners of bank purchaser. It should also be noticed that the acquisition of a smaller or less efficient bank helps to diversify income better and thus create value rather than the acquisition of a bank which is liquid but has a higher credit risk. Altunbas and Ibáñez (2004) in their research state that mergers and acquisitions in the banking sector have increased banks' capital return, because an opportunity emerged to efficiently differentiate the bank resources. However, the differences between endogenous and international transactions should be noticed: creating endogenous translations there is a problem to integrate different institutions according to their strategies of loans, income, expenditures and deposits management; international transactions of mergers and acquisitions, though can be characterised by different separate institutions' loans and credit risk management strategy, but still adds to the greater efficiency of a merged bank. Valkanov and Kleimeier (2007) state that in terms of bank mergers a greater value is created if the bank's target capital rates exceed the rates of the bank's purchaser. The authors also state that bank capital quality is reflected in the fluctuations of the stock market price what affects the merger.

Hitt *et al.* (2012), Dutordoir *et al.* (2014), analysing the created value of mergers and acquisitions, provide that mergers and acquisitions can create little value or no value at all. One of the main reasons due to which no synergy is created is the one that the seller overpays for the bank acquired when wrong aims and inefficient integration processes are selected. It should be noticed that only selected aims and efficiently implemented acquisitions can achieve the interaction and create added value. It should be noticed that synergy is one of the main reasons of mergers and acquisitions in the banking sector. Being a business company and having its shareholders, a bank strives for financial synergy (return). Financial synergy can be achieved by optimising the performance of the merged banks with the achievement of the economy of scale, market power, the efficient use of expenditure etc. This aim is most likely to be achieved by implementing the mergers of separate institutions or just acquiring other ones and thus striving for the efficiency. However, it is stated that such aim of a finance subject – a bank – cannot always be combined with the aim of the market or that of separate institutions to guarantee the financial stability. This issue becomes especially relevant assessing *too-big-to-fail* risk (Mishkin 1999). This is why such consolidation can cause the opposite effect, i. e. reduce the market efficiency and cause anticompetitive environment (Sood, Ahluwalia 2009).

Thus *the aim* of the current article is to analyse the reasons of bank mergers and acquisitions which have taken place in Lithuania during the period of independence and to define whether the merged banks have created value for shareholders and (or) the financial system. The second part of the article provides research methodology and describes the scope of the research. The third part of the article provides the results of the research which include the evaluation of four bank mergers and acquisitions that have taken place in Lithuania.

2. Data and research methodology

The analysis of mergers and acquisitions in the Lithuanian banking sector in the context of value creation has been carried out using case research methodology. This qualitative research allowed a separate interpretation of the issue analysed and provided the opportunity to holistically view the problem of the research. The scope of the research consists of bank mergers and acquisitions that have taken place in the period of 1990-2013: the merger of AB Vilniaus bankas and AB Hermis bank, the restructuring of AB Lietuvos valstybinis komercinis bankas (with the participation of AB Lietuvos taupomasis bankas), the acquisition of AB Finasta bank (by AB Snoras bank) and the restructuring of AB Ūkio bank (with the participation of AB Šiaulių bank). This option was determined by the theoretical assumption that consolidation takes place when several members of the market merge together and due to such a merger or acquisition one market member is formed, in the analysed case – one bank.

Dermine (2009, 2010) provides one of the most detailed methods determining bank value. He states that in order to create value in the bank's activities, first of all it is necessary to define and understand the functioning of value creating agents. Dermine (2009) provides that there are four methods used in determining bank value: a) market multiplier method, b) future divided discount value method c) economic profit value method d) "fundamental" value determination method. In order to define the financial synergy and the value of Lithuanian bank mergers economic profit (or *EVA – economic value added*) value method. EVA estimate was created and developed by Joel M. Stern and G. Bennett-Stewart III, they defined the economic profit as the difference between net operating profit after tax (NOPAT) and capital expenditures (1998):

$$EVA = NOPAT - (IC \times WACC), \qquad (1)$$

here: NOPAT – net operating profit after tax; IC – invested capital; WACC – weighted average cost of capital.

Economic profit can also be calculated as the multiplication of the invested capital and the difference of the return on invested capital and weighted average cost of capital:

$$EVA = (ROIC - WACC) \times IC, \quad (2)$$

here: ROIC – return on invested capital.

main problem calculating the economic benefit arises due to the limited possibilities to define the price of the equity. With the application of this method, the main problems are associated with the evaluation of the value created by finance intermediaries. It is especially important to emphasise that bank's net operating profit after tax is calculated by taking away extraordinary activity result and non-financial articles result (e. g. formed loan provisions, tax provisions etc.) from the net value. The calculation of this index is affected by the fact that subordinated liabilities are kept together with net asset and clients' deposits are not evaluated as their price (expenditures to attract them) are evaluated with NOPAT indicator.

In order to calculate the equity price of the analysed banks the methodology proposed by Geretto and Mazzocco (2010) was used. P/E ratio (market price per share divided by earnings per share) was used to calculate the equity price. However, this method has several restrictions of application as well. Though the ratio combines two variables: balance value (net asset) and market value (price per share), there are, however, possible market distortions arising due to future profit expectations from the members of the market (the expected rise of profit raises the price per share and this tendency reduces E/P ratio). Thus a situation is formed when with the same amount of the profit the equity price decreases. In such a case, with the applied adjustments of EVA calculation methodology for a bank, the economic profit is calculated as follows:

$$EVA = (ROE - r_e) \times E. \quad (3)$$

The main difference between formulas (1), (2) and (3) is that instead of the amount of the return on invested capital the difference between equity return and equity price is used. It emphasises the main differences between bank capital and other companies' capital structure. With banks' merger or acquisition the changes of value are evaluated comparing *ex-ante* data of two separate business subjects before the merger/acquisition with *ex-post* (after merger/acquisition) data. If EVA result of the new (merged) bank is larger than EVA sum of the two separate institutions, the merger/acquisition which has taken place has created economic added value.

Concentration ratios were used to establish bank consolidation effect on the financial system. *"k" concentration ratio* evaluates the part of the market occupied by the largest banks. Most commonly CR_3 and CR_5 concentration ratios are applied. However, CR_1 ratio is used in the research in order to define the effect of the merging banks and the bank merger (the occupied part of the market) on the market.

"k" concentration ratio is calculated according to the following formula (Bikker, Haaf 2000):

$$CR_n = \sum_{i=1}^{k} S_i \;, \quad (4)$$

here: k – the number of banks, si – the market share of i bank.

Another index used to evaluate the effect of the merged banks is *Herfindahl – Hirschman index (HHI).* It is the concentration index that is most commonly used in theoretical literature, as the measure for other concentration evaluating indices. HHI index is calculated as the sum of the squares of the market shares of the bank sizes. HHI is calculated according to the following formula (Bikker, Haaf 2000):

$$HHI = \sum_{i=1}^{n} S_i^2, \quad (5)$$

here: S_i – the market share of the bank.

When HHI < 1000, market concentration level is not high; when 1000 < HHI < 1800, market concentration level is average, when HHI > 1800, market concentration level is high.

3. Research results

3.1. AB "Vilniaus bankas" and AB "Hermis" bank merger analysis

The analysis of this translation shows that when AB "Vilniaus bankas" declared its plan to acquire AB "Hermis" bank, its economic value index was the highest and reached almost LTL 26 million and AB "Hermis" bank's economic profit was slightly above LTL 1 million. With the acquisition of AB "Hermis" bank by AB "Vilniaus bankas", the economic value of the merged bank decreased and became negative (see

Table 1). It can be stated that the merger brought no benefit for the merged bank. However, the later data shows that the economic added value of the merged bank increased and almost reached the value of AB "Vilniaus bankas" before the merger. Thus it can be stated that there was one-year gap during which the merged bank used the synergic effect created by the merger and realised additional benefit acquiring the bank, what influenced the growth of the economic benefit[1]. However, the later results of the merged bank activity show that the economic value decreased.

Table 1. Economic value added of AB "Vilniaus bankas" and AB "Hermis" bank

Year	Return on equity (ROE)	Equity price, (K_e)	Amount of the equity capital, thousands LTL (E)	EVA, thousands LTL
$EVA = (ROE - K_e) \times E$				
AB Vilniaus bankas				
1998	0,2595	0,1993	435.445	**26.213,789**
1999	0,1602	0,1928	513.666	-16.745,512
2000	0,1519	0,108	585.764	**25.715,04**
2001	0,1506	0,121	684.707	**20.267,327**
2002[2]	0,1694	0,1559	811.213	**10.951,375**
2003	0,152	0,1403	943.489	**11.038,82**
2004	0,12	0,1132	1.064.001	**7.235,21**
AB "Hermis" bank				
1998	0,02	0,012	148.707	**1.189,656**

Source: composed and calculated by the authors, on the basis of (AB "Vilniaus bankas": Financial Statements: 1999, 2000; Annual Report 2001; AB "Vilniaus bankas": Financial Statements: 2002, 2003; AB "Vilniaus bankas": Financial Statements: 2003, 2004; AB SEB "Vilniaus bankas": Annual Report 2004, 2005; AB "Hermis": Annual Report 1998, 1999)

In order to evaluate the effect of this transaction on the financial system market concentration indexes were calculated. It can be noticed that in 2000 the market share of AB "Vilniaus bankas" assets, loans and deposits exceeded 40 percent. The Law on Competition of the Republic of Lithuania provides that the economic subject occupies a dominating position in the market if its market share composes at least 40 percent, thus AB "Vilniaus bankas", acquiring AB "Hermis" bank, occupied the leading position in Lithuanian banking market, what allowed it to take the advantage of synergy. Later, AB "Vilniaus bankas"' domination in the market gradually reduced, however, it was close to 40 percent (see Fig. 1). AB "Hansa-LTB" became the main competitor for AB "Vilniaus bankas", when in 2001 AB "Lietuvos taupomasis bankas" was privatised, i. e., acquired by a daughtering foreign bank "Hansabankas".

[1] Synergic effect is when
EVA merged bank > EVAVB + EVAHERMIS

[2] 2002 and subsequent years AB "Vilniaus bankas" share price is measured in calculating the carrying value of the shares price as AB "Vilniaus bankas" shares were included in the Lithuanian National Stock Exchange till February 1, 2001.

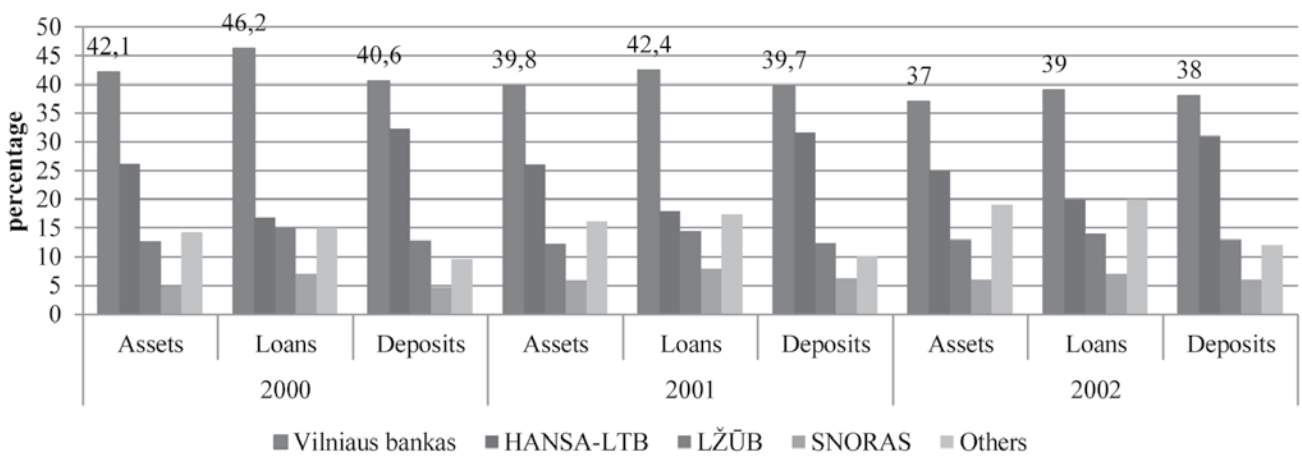

Fig.1. Operating banks share in Lithuania's market in 2000-2002

Source: composed and calculated by the authors, on the basis of (AB "Vilniaus bankas": Report 2001; AB "Vilniaus bankas": Financial Statements 2002, 2003)

It is important to mention that any merger or acquisition first of all should be beneficial to shareholders, because without their agreement and intention such a transaction is not carried out. Thus the shareholders' intention to develop, increase the influence on the market, the number of clients and the circle of the services provided ensures the opportunity for mergers and acquisitions to take place on the market. After the calculation of economic value added of both banks it can be observed that when AB "Vilniaus bankas" acquired AB "Hermis" bank, its EVA estimate deteriorated a lot and became negative (LTL -16.745 thousand), and the economic value of the bank grew instantly in one year. This growth could be justified by the received synergy effect: when the banks merged, the management structure, the network of the branches was optimised, the information basis was integrated, a perspective to found new companies, providing additional services appeared, monopolistic position on the market allowed to use the power to govern interest margin, increase the number of clients and the circle of the services provided. After the banks were merged and the capital increased, there were the conditions to provide the market with larger loans, the demand for which was especially felt at that time. Moreover, the participation of AB "Vilniaus bankas" strategic investor in the transaction and its pursue allows making an assumption that AB "Hermis" bank's acquisition by AB "Vilniaus bankas" was supposed by the agents determining long-term mergers and acquisitions: the acquired dominating position on the market and *too-big-to-fail* benefit.

However, this merger of two banks which took place in Lithuania and ended up with the acquisition of AB "Hermis" bank, had negative effects as well: first of all, the process of merger/acquisition was very long (almost 2.5 years), during which the board of AB "Hermis" bank opposed the transaction by all possible means, what had negative effects on the bank itself: there were mistakes in granting loans, assessing the accepted risk; all this determined a relatively worse asset value and later allowed AB "Vilniaus bankas" to form a great prestige of the acquired bank.

It is difficult to provide a single evaluation of the merger of these two banks. It is assumed that the Bank of Lithuania should have not approved of the merger of these two banks, AB "Vilniaus bankas" and AB "Hermis" bank, because the market share governed by both of them increased a lot (see Table 2). When the new bank acquired the dominating position on the market, it could actively govern the equity interest rates, to establish and dictate interest rates, commission fees for the bank's provided services; the merged bank also acquired an opportunity to provide syndicated loans and attract large clients. Such a situation on the market strengthened the struggle for large clients and other banks became unsatisfied due to small possibilities to compete with the merged bank.

Table 2. Indicators of banks market concentration in 1998

		January 98	March 98	June 98	September 98	December 98	December 98*
HHI	**Assets**	2.128	2.117	2.066	2.105	2.143	**3.068**
	Loans	2.183	2.077	2.07	2.063	2.035	**3.178**
	Deposits	2.325	2.257	2.228	2.298	2.264	**2.977**

Note. In the period marked by the asterisk (*) AB "Vilniaus bankas" and AB "Hermis" bank are regarded as one merged bank.

Source: Navickas (1999)

3.2. Analysis of the reorganisation (acquisition) of AB Lietuvos valstybinis komercinis bankas

The restructuring of AB Lietuvos valstybinis komercinis bankas (hereinafter – LVKB) is important because it is closely associated with the baking sector and the entire finance sector stability. It is established that LVKB assets before the restructuring reached LTL 0.8 billion, loans portfolio composed LTL 0.6 billion of which (see Table 3). In 1997 LTB was one of the major Lithuanian banks with 22 percent of assets, 14 percent of loans and 26 percent of deposits market. After the "good" part of LVKB assets and liabilities was taken over, LTB market share increased and composed 38 percent of the assets, 27 percent of loans and 39 percent of deposit market, and it became the largest in Lithuania (only AB "Vilniaus bankas" had 30 percent of loan market) (see Fig. 2).

On April 30, 1998 the Government accepted a decision to liquidate LVKB (On AB "Lietuvos valstybinis komercinis bankas" liquidation, 1998). Finally, on July 1, 1999, the Board of the Bank of Lithuania decided to exclude LVKB from the Companies' Registration Office of the Republic of Lithuania (On Lietuvos valstybinis komercinis bankas AB exclusion from the Companies' Registration Office of the Republic of Lithuania, 1999), and at the beginning of 2001 AB "Lietuvos taupomasis bankas" was sold.

The start of the concentration in the banking sector was the restructuring of LVKB and giving over part of its assets and liabilities to LTB. The calculated HHI index shows that the concentration in the part of assets increased from 0.1602 to 0.3271 points, in the part of liabilities it increased from 0.1740 to 0.2671 points, and in the part of deposits it increased from 0.164 to 0.26 points (see Fig. 2). Thus it can be stated that Lithuanian banking market has become very concentrated.

Table 3. Performance results of AB "Lietuvos valstybinis komercinis bankas" and AB "Lietuvos taupomasis bankas"

Year	Assets, thousands LTL	Loans portfolio, thousands LTL	Amount of the equity capital, thousands LTL	Deposits portfolio, thousands LTL
AB Lietuvos valstybinis komercinis bankas				
1996	856.800	616.700	165.000	544.200
1997	778.000	599.300	**-122.600**	598.700
AB Lietuvos taupomasis bankas				
1996	1.184.600	505.000	40.000	1.015.200
1997	1.839.600	591.100	81.600	1.526.800
Results of AB Lietuvos taupomasis bankas after acquiring "good" share of AB Lietuvos valstybinis komercinis bankas assets and liabilities				
1998	3.212.100	1.067.900	235.000	2.282.900

Source: composed and calculated by the authors, on the basis of the Bank of Lithuania's monthly statements (1996-1997; 1998)

Thus this case of the bank acquisition (restructuring) can be a particularly important example connecting bank acquisition process and finance system stability. In order to reduce the hazard of "infection" in the financial system, the government recapitalised the bank and, despite the failure to successfully sell the bank, restructured it. This case also proves one of "concentration-stability" hypotheses, raised in scientific literature, when bank activity reform was chosen by restructuring it (incorporating part of the bank's assets and liabilities into another bank). After overtaking part of LVKB activity, LTB became important and large and the banking sector became highly concentrated. However, it can be noticed, that LTB, after increasing its market share, became a large and important bank on Lithuanian market. It is observed that such restructuring of the bank's activities increased the assets of the acting bank significantly, and also ensured its opportunity to actively compete on the market and to use the benefit of the synergy: to optimise the management structure and to provide new services on the market.

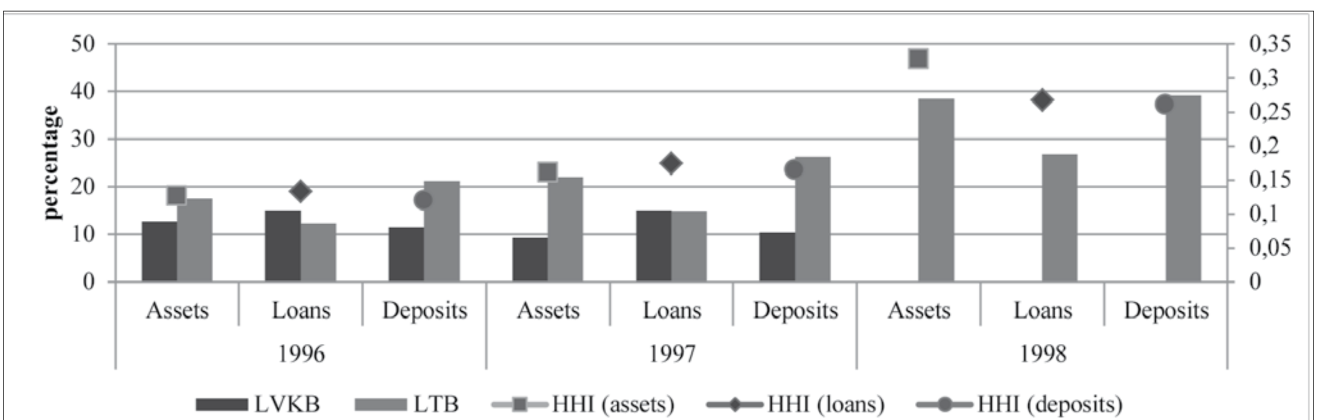

Fig.2. Market share of AB "Lietuvos valstybinis komercinis bankas" and AB "Lietuvos taupomasis bankas" and market Herfindahl-Hirschman index (right scale) 1996 – 1998

Source: composed and calculated by the authors, on the basis of the Bank of Lithuania's monthly statements (1996-1997; 1998)

3.3 AB "Finasta" bank acquisition analysis

The newest and the most unique example of a bank acquisition in Lithuania's banking history took place on 16 September, 2009, when AB "Snoras" bank group completed the transaction during which it independently acquired 100 percent of shares of AB "Finasta įmonių finansai", governing AB "Finasta" bank from AB "Invalda" and 100 percent of shares of the companies AB FMĮ "Finasta", UAB "Invalda turto valdymas" and IPAS "Invalda Asset Management Latvia". This bank acquisition is analysed in more detail because AB "Finasta" bank acquisition took place by establishing holding and later, the activity of the bank purchaser, AB "Snoras" bank, raised a certain public resonance: the purchaser bank was denied the activity licence and the management of this bank's shares was transmitted to the state.

The evaluation of AB "Finasta" bank acquisition by EVA method is difficult, because in 2008 AB "Finasta" bank experienced a LTL 3.88 million loss; in 2009 the loss was LTL 6.71 million; in 2010 the bank made LTL 89 thousand net profit (AB FINASTA bank: 2009 financial reports, 2010; AB FINASTA bank: 2010 financial reports, 2011). AB "Snoras" bank's activity results in 2007-2011 second quarter were also rather poor: in 2007 the bank made LTL 71.7 million net profit, however since 2008 the bank's profit decreased and made about LTL 22 million, in 2009 LTL 8.7 million of net profit, in 2010 LTL 9.9 million and in 2011 second quarter – LTL 7.1 million of net profit (see Table 4). However, calculating the effect of AB "Finasta" bank's acquisition on AB "Snoras" bank by EVA estimate, it has been established that AB "Snoras" bank capital price exceeded capital return (see Table 5).

Table 4. Performance results of AB "Snoras" bank and AB "Finasta" bank

Year	Assets, LTL thousands	Loans portfolio, LTL thousands	Amount of equity, LTL thousands	Deposits portfolio, LTL thousands	Net interest income, LTL thousands	Return on assets (ROA), per cent	Return on equity (ROE), per cent
AB "Snoras" bank							
2008	5.694.651	3.425.752	495.120	3.905.418	99.662	**0,386**	**4,43**
2009	6.342.578	3.269.786	505.009	4.994.204	4.043	**0,137**	**1,72**
2010	7.656.346	4.220.429	597.253	6.346.562	81.144	**0,13**	**1,66**
AB "Finasta" bank							
2008	53.025	31.491	15.314	34.272	1.430	**-7,32**	**-25,34**
2009	73.974	25.292	21.382	49.371	2.297	**-9,07**	**-31,36**
2010	188.757	42.572	21.471	110.537	4.792	**0,03**	**0,27**
2011	288.577	49.980	5.286	71.222*	7.874	**-9,07**	**-495,37**
2012	363.812	56.823	19.282	125.948*	10.817	**-0,4**	**-7,55**

* In 2011 AB FINASTA bank additional has 192.5 million LTL and in 2012 – 191.1 million LTL deposits of other credit institutions.

Source: composed and calculated by the authors, on the basis of (AB bank "Snoras" Financial Statements 2008, 2009; AB bank "Snoras" Financial Statements 2009, 2010; AB bank "Snoras" Financial Statements 2010, 2011; AB bank "Finasta": Financial Statements 2009, 2010; AB bank "Finasta": Financial Statements 2010, 2011, 2012, 2013)

The dynamics of the indices shows that AB "Snoras" bank acquiring AB "Finasta" bank tried to "hide" the inefficiency of its activity and through this transaction ("Finasta" financial group acquisition), the bank hoped and could strengthen its activity in the field of investment banking and assets management, offering the clients high qualification specialists' services in companies' finance, investments, assets and welfare management. Moreover, due to this translation AB "Finasta" bank gained the opportunity to provide the services and spread the products through the largest at that time Lithuanian network of clients' services and offer new products. This synergy opened AB "Snoras" group the opportunities to raise the managed assets and the number of customers in retail and investment banking sectors in Lithuania and abroad. Thus, through this transaction AB "Snoras" bank broadened its market, raised assets and thus tried to become a *too-big-to-fail* bank and acquire more trust of the market members. However, it can be stated that AB "Snoras" bank acquired AB "Finasta" bank reaching for financial and non-financial synergy.

Table 5. Economic value added of AB "Snoras" bank and AB "Finasta" bank

Year	Return on equity (ROE)	Equity price, (K_e)	Amount of the equity capital, thousands LTL (E)	EVA, thousands LTL
EVA = (ROE – K_e) x E				
AB "Snoras" bank				
2007	0,1422	0,0518	504.484	**45.605,354**
2008	0,0443	0,1316	495.120	**-43.223,976**
2009	0,0172	0,022	505.009	**-2.418,993**
2010	0,0166	0,0226	597 253	**-3.571,57**
2011 m. II ketv.	0,0091	0,0132	791.150	**-3.212,069**
AB "Finasta" bank				
Considering the fact that during its activity period AB "Finasta" experienced loss and its return on equity (ROE) and other indices (EPS, K) are negative, in its case EVA estimate calculation is not applicable.				

Source: composed and calculated by the authors, on the basis of (AB bank "Snoras" Financial Statements 2008, 2009, 2010, 2011; AB bank "Finasta": Financial Statements 2009, 2010, 2011)

After the acquisition, AB "Finasta" bank acted as a separate legal entity, 100 percent of the equity of which was governed by AB "Snoras" financial group. It can be noticed that this transaction had no particular effect on the concentration of the banking market, because AB "Finasta" bank's acquisition was dedicated to broaden the field of investment banking services provided by AB "Snoras" bank. It can also be stated that AB "Snoras" bank's market share (assets, loans and deposits) has not considerably changed after the transaction, what can also be observed in table 4: AB "Finasta" bank had approximately LTL 63 million assets, about LTL 30 million loans and about LTL 40 million deposits, and AB "Snoras" bank had more than LTL 6 billion assets: above LTL 3 billion loans and LTL 5 billion deposits. However, a successful bank's acquisition[3] and its possible positive synergy have not ensured the existence of the bank's purchaser. Due to wrong management of the bank's activity risk and its negative effect on the bank's activity, on August 22, 2012 by the decision of Vilniaus apygardos teismas, AB "Snoras" bank liquidation procedure was commenced.

[3] It can be stated that AB "Finasta" bank's acquisition was the right step of AB "Snoras" bank. It can be observed from EVA estimate change. It is noticeable that economic value added of the merged bank, though was negative, but decreased. Of course, it cannot be stated that this transaction had direct positive effect on EVA estimate. However, additional dispersal of the bank's performance and the diversification of the earned income improved EVA estimate.

3.4. Analysis of restructuring AB "Ūkio" bank and AB "Šiaulių" bank

The newest significant change in the Lithuanian finance system is AB "Ūkio" bank restructuring, which took place at the beginning of 2013. The case is significant because it can be associated the Bank of Lithuania's intention to ensure the stable activity of the banking sector. Analysing the main performance results of AB "Ūkio" bank (see Table 6), it can be observed that in 2010 the bank has experienced loss from its main activity (loan provision) (LTL -3.48 million); this result shows the inadequate management of the bank's activity (especially credit and interest rates) risk. Later (from 2011) banks net interest income increased and reached approximately LTL 48 million. The bank's main activity indexes (assets and return on equity, as the bank experienced loss), in 2010-2012 3rd quarter were negative. The bank's loans portfolio has almost remained the same and through the analysed period composed LTL 2.3 billion. A large part of the bank's assets consisted of investment assets (almost half of the assets). Deposit portfolio in 2010-2012 3rd quarter decreased 11 percent; at the end of 2012 3rd quarter, AB "Ūkio" bank's capitalisation composed LTL 131.3 million, and AB "Šiaulių" bank's capitalisation – LTL 187.3 million. It is important to mention that AB "Ūkio" bank's and AB "Šiaulių" bank's loans portfolios were similar. The main difference was that AB "Ūkio" bank's assets 1.5-2 times exceeded AB "Šiaulių" bank's assets. This difference mainly formed due to AB "Ūkio" bank's investment assets.

However on 12 February, 2013, the Board of the Bank of Lithuania declared AB "Ūkio" bank's activity restrictions (Temporary restrictions of "Ūkio" bank's activity, the appointment of temporary bank's administrator, 2013; On the approval of the recommendations and conclusions provided by AB "Ūkio" bank's temporary administrator and AB Ūkio bank insolvency and the withdrawal of the banking licence, 2013). Thus it was decided that AB "Šiaulių" bank will takeover the AB "Ūkio" bank's commitments to its clients, not exceeding the insurance remuneration provided in the Law on Insurance of Deposits and Liabilities to the Investors of the Republic of Lithuania. According to the approved preliminary asset evaluation the general sum of the client's liabilities transferred to "Šiaulių bankas" made LTL 2.7 billion. The value of the transferred assets (LTL 1.9 billion) and VĮ "Indėlių ir investicijų draudimas" deposit value (LTL 0.8 billion) was equal, LTL 2.7 billion (The signed agreement on transferring Ūkio bank commitments and assets to "Šiaulių" bank, 2013). The remaining part of "low quality" assets remained in "bad" AB "Ūkio" bank. Also, after auditing AB Ūkio bank's financial results, it was established that after the transfer of liabilities and assets, AB "Ūkio" bank's net asset value is LTL 356.322 million, liabilities – LTL 1 583.14 million, i. e., net asset value is LTL 1 226.82 million lower than the liabilities, thus the bank remains insolvent (The Bank of Lithuania will commence the proceedings on the bankruptcy case for "Ūkio" bankas, 2013). Thus the board of the Bank of Lithuania decided to appeal to the court on commencing the bankruptcy proceedings against AB "Ūkio" bank. On May 2, 2013, the bankruptcy proceedings against AB "Ūkio" bank were commenced and temporary bankruptcy administrator was appointed (Bankruptcy proceedings against AB "Ūkio" bank, 2013).

The analysis of the Lithuanian banking market share of both banks shows that before the termination of its activity, AB Ūkio bank had a greater market share of assets, loans and deposits than AB Šiaulių bank (see Fig. 3). Both banks had a similar market power only on the loans market. Anyway, after AB Šiaulių bank acquired a "good" part of AB Ūkio bank's assets and liabilities, its market influence increased, especially AB Šiaulių bank's deposit market share: it increased from 4.7 pecent to 10.2 percent; the deposit portfolio increased 114 percent (till LTL 4.6 billion). AB Šiaulių bank's assets also increased (due to the overtaken AB Ūkio bank's good quality investment assets).

Thus the division of one unsuccessful bank's activity provided the opportunity for the bank which overtook the assets to acquire market power and take advantage of the bank's size. Another important evaluated aspect is banking market concentration. The calculation of HHI index shows that after the reorganisation of AB "Ūkio" bank's activity, the concentration on the market increased insignificantly. The assets on the market increased from 0.19 to 0.201, the loans – from 0.192 to 0.218, the deposits – from 0.201 to 0.218. Thus the current Lithuanian banking market is of average concentration level. Additionally, it can be mentioned that in this case "concentration-stability" hypothesis has partially been confirmed.

In order to achieve the stability of the financial system (and the financial sector as well) (On the approval of the recommendations and conclusions of AB "Ūkio" bank's temporary administrator and AB "Ūkio" bank's insolvency and bank's licence termination, 2013), the board of the Bank of Lithuania has decided to partially increase the concentration on the market, but in this way to retain the stability of the financial system. "Standard & Poors" ranking agency is of the same opinion. The agency, after the decision of the board of the Bank of Lithuania to reorganise AB "Ūkio" bank's activities, published the report which stated that "the restructuring of the collapsed "Ūkio" bank by transferring part of its liabilities and assets to "Šiaulių" bank, will not have any effect on Lithuania's credit rating, because Ūkio bank was mainly financed from deposits, the part of which in the common system did not reach 8 percent, the agency does not hope that the likely bank's restructuring will affect the financial stability of Lithuania's banking sector" ("Standard & Poors": "Ūkio" bank's restructuring will not affect Lithuania's credit rating, 2013).

Table 6. Performance results of AB "Ūkio" bank and AB "Šiaulių" bank

Year	Assets, LTL thousands	Loans portfolio, LTL thousands	Amount of equity, LTL thousands	Deposits portfolio, LTL thousands	Net interest income, LTL thousands	Return on assets (ROA), per cent	Return on equity (ROE), per cent
AB Ūkio bank							
2010	4.923.246	2.287.838	405.030	3.962.918	**-3.479**	**-0,83**	**-9,51**
2011	4.220.417	2.282.394	452.218	3.438.435	55.264	**-0,1**	**-1,06**
2012 m. III ketv.	4.094.363	2.230.654	406.622	3.526.626	41.927	**-1,17**	**-11,76**
AB Šiaulių bank							
2010	2.334.654	1.657.609	256.147	1.672.394	28.839	**-1,1**	**-9,47**

2011	2.731.566	2.069.758	297.608	1.894.167	50.051	**0,49**	**4,61**
2012	2.931.466	2.052.809	318.856	2.165.852	55.430	**0,52**	**4,79**
Results of AB Šiaulių after acquiring "good" share of AB Ūkio bank assets and liabilities							
2013 m. I ketv.	5.422.443	2.721.293	322.128	4.640.396	11.016	**0,06**	**1,06**
2013	5.250.828	2.723.648	321.225	4.586.362	83.039	**0,22**	**3,36**
2014 m. I ketv.	5.297.103	2.633.802	340.858	4.573.294	28.139	**1,22**	**19,77**

Source: composed and calculated by the authors, on the basis of (AB "*Ūkio bankas*" Annual Report 2011, 2012; AB Ūkio bankas Nine-month interim report 2012; AB "*Šiaulių bankas*": 2010 m. Auditor›s Report, Financial Statements and Annual Report 2011; AB "*Šiaulių bankas*": Auditor›s Report, Financial Statements and Annual Report 2013; AB "*Šiaulių bankas*" 2013 m. Quarterly financial report 2013)

International Monetary Fund in its report (IMF Executive Board Concludes 2013 Article IV Consultation with Republic of Lithuania 2013), also positively evaluated the Bank of Lithuania's solution of the problems of this bank. According to the IMF, the decisive actions of the state's institutions have strengthened the credibility of all the financial system. The IMF also notes that current Lithuanian banking sector has enough capital and liquid assets stocks.

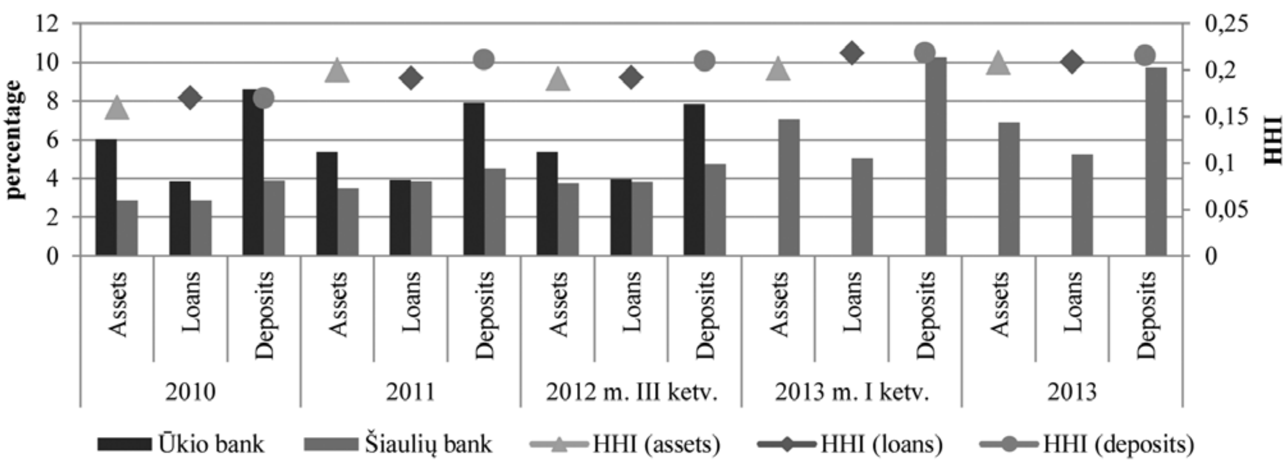

Fig.3. Market share of AB "Ūkio" bank and AB "Šiaulių" bank and market Herfindahl-Hirschman index (right scale) 2010 – 2013 1st quarter

Source: calculated and composed by the authors, on the basis of Main banks activity ratio 2010-2013 I quarter

In conclusion it can be stated that the reduced number of the market agents first of all determines a larger market concentration which is not always favourable for the customer. However, it would be incorrect to state that market concentration always increases when banks merge, because the acting banks can specialise in different market segments and thus not raise the competition. AB "Hermis" and AB "Finasta" banks' acquisitions were made in order to make value for their acquisitors – AB Vilniaus bankas (its strategic investor – SEB) and AB "Snoras" bank. The *Too-big-to-fail* concept cannot be rejected as well, because new banks (especially in the first case) have expanded the part of the market share and became important parts of the financial system. It should be noted that AB "Hermis" bank's acquisition was affected by the intention to ensure the stability of the financial system. However, it should be remembered that a bank, though being a systematically important institution, is also a profit institution, thus the aim of strategic shareholders to receive financial benefit is always implemented (the result of this transaction: in short term – financial system stability; in long term – shareholder's return).

Analysing the current Lithuanian banking market it can be presumed that mergers and acquisitions can take place in the nearest time in order to develop and (or) optimise the activity. At the beginning of 2013, "Ūkio" bank's activities were terminated and the bank's assets, rights, transactions and liabilities were transferred to other bank of Lithuania – "Šiaulių" bank. It should be noted that AB "Šiaulių" bank, after the acquisition of the "good" AB Ūkio bank's assets, could become an attractive bank for foreign investors and most probably the member of the acquisition. Moreover, the aim of one of the main shareholders of AB "Šiaulių" bank, the European Bank for Reconstruction and Development, is not a long-term participation in the bank's capital, but the strengthening of the bank's performance and the recovery of the invested funds in case of possible bank selling.

Though the aim of the processes of the bank consolidation in Lithuania was to ensure the stability of the financial system, there is still observed particular domination of the bank's acquisitor in the transaction. AB "Vilniaus bankas" currently belongs to one of the largest Scandinavian financial group SEB, AB "Lietuvos taupomasis bankas" was acquired by AB "Hansabankas", which later became a subsidiary of the Swedish bank Swedbank. Both these banks acting on the Lithuanian market constitute about 50 percent of the bank's assets market (together with the third bank, acting in Lithuania, a Norwegian finance group DNB subsidiary bank they constitute 74 percent of the market (Main banks activity ratio, 2014)). It should be mentioned that there are two branches of Scandinavian banks, "Nordea" and "Danske", in Lithuania, which constitute about 16 percent of Lithuanian banks' assets market. Thus modern Lithuanian banking market is closely related to the Nordic European financial sector. On 27 July, 2008, The Ministry of Economy of the Republic of Lithuania provided the Government of the Republic of Lithuania with the Economic security strengthening project in which indicated that "Lithuanian banking sector is very concentrated and dependent on one foreign region's banks (investors from Scandinavia through their subsidiaries occupy about 68.7 percent of the market), thus financial problems of the Nordic countries' market can affect the stability of Lithuanian banking activity. On the one hand, the domination of Scandinavian banks which are financially strong and of good reputation contributes to the development of the national banking sector and financial services (and all the economy) and increases the stability. The commitment declared and actually proved by these institutions to pursue a responsible and long-term oriented activity in the Baltic region strengthens the ability of Lithuanian banking sector to act in a less advantageous domestic economic environment, sustain general shocks of financial markets. On the other hand, however, the problems of patronising banks in Nordic countries would also affect their subsidiary banks in Lithuania". Thus such a close relation of Lithuanian banking sector with a single foreign region is dangerous. The government of the Republic of Lithuania is suggested to consider this situation and form a long-term strategy of the Lithuanian financial sector, the result of which would be the creation of a banking sector not dependent on one global region. The Bank of Lithuania has recently suggested the acting credit unions to unite to form cooperative banks, as this would increase the unions' competitiveness, strengthen their capital and management quality and together would be an alternative for the Scandinavian banks dominating in Lithuania. The experience of the countries with long banking traditions, such as Switzerland, should not be forgotten. The country has many local banks (e. g. Raiffeisen Bank, Kantonalbanken, Regionalbanken), which are independent of other countries' banks and able to sustain the liability of non-finance companies and households during the economic decline and significantly reduce debt service expenditure, what is necessary for the economic incentive. It should be noticed that an individual country's economic and financial independence depends on its possibility to freely provide itself with the necessary resources (have a financial institution managed by the country's own capital, which would be able to contribute to the implemented economic policy).

Conclusions

The mergers and acquisitions in the banking sector are determined by tangible and intangible synergy agents. The main motives for such transactions depend on the state's economic situation. It should be noticed that the most common reason for bank mergers is economic benefit for the banks: to raise shareholders' revenue and benefit. The aspect of financial stability in mergers and acquisitions emerges in short term and is most often determined by the state government's actions; in long term, however, financial benefit motive dominates.

It should be noticed that the first analysed merger in the banking sector, which ended up with the acquisition, is unique and complicated. AB "Vilniaus bankas" and AB "Hermis" bank's merger significantly increased market concentration, acquired monopolistic position on the market and could benefit from it seeking for additional value. However, all these possible negative aspects had positive effects as well: the strategic investor from the Nordic state, Swedish SEB bank enriched Lithuanian baking sector with new labour culture, standards of ethics, the peculiarities of the communication with the clients etc. The new bank gave an impulse for the national economy and could also provide the country with new services, which had been poorly developed or not developed at all. It could also be partially stated that the acquisition ensured the stability of the financial sector because the result of the transaction was a great prestige which was formed revaluing the assets (loans portfolio) of the acquired bank.

AB "Lietuvos valstybinis komercinis bankas" restructuring is distinguished by its uniqueness and specificity. Such a transaction is not essentially a typical merger or acquisition. However, it was important for Lithuanian economy in order to ensure a stable activity of financial sector. Due to its difficult situation, "Lietuvos valstybinis komercinis bankas" was split and qualitative bank's assets were transferred to AB "Lietuvos taupomasis bankas", acting at that time. The "bad" part of the bank's assets was transferred to AB Turto bank. Such a conclusion of the bank's division transaction helped to reduce the fluctuations of Lithuanian financial sector's stability.

AB "Snoras" bank acquired AB "Finasta" bank in order to reach financial and non-financial synergy, especially providing the clients with the new services: companies' finance, assets and welfare management. However, the successful acquisition of the bank and its synergy did not ensure the activities of the bank's acquisitor, thus it can be stated that, due to its ineffective activity, AB "Snoras" bank was declared bankrupt and the bank was liquidated.

The newest restructuring of AB "Ūkio" bank's activity on Lithuanian market has shown that the division of the bank's activity (dividing its assets and liabilities into "good" and "bad") can be the right measure to ensure the stable activity of the financial system. Moreover, such division of one unsuccessful bank's activity provided the bank which overtook the assets with the opportunity to acquire market power and take advantage from the bank's size.

The recommendations for the Government of the Republic of Lithuania would be to pay attention to the concentration of the banking sector which includes its dependence on the banks of one foreign region. This dependence can be dangerous during the time of economic instability, when the "contamination effect" (or the systematic risk) spreads more easily. The domination of one region's banks is especially dangerous because the lack of trust in the financial sector could spread fast to markets and negatively affect the economy of the state.

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