

Banking Mergers and Acquisitions' Performance and executive compensation in Europe

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Abstract

In this paper, we investigate whether managerial power and experience of executives influences M&A performance and whether there is a linkage between M&A performance and executive compensation. The aim is to understand if any causality relationship exists among executives power, bank performance and their compensation in Europe. To assess banking performance, and CEO compensation we use OLS regression model on 52 bank-to-bank M&A from EU15 countries plus Norway and Iceland. We find a positive significant relationship between managerial power and post deal bank performance.

Jel classification: G21, G30, G34

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1. Introduction

The European banking sector has experienced a rapid process of mergers and acquisitions (M&A) during the 1990s³. The deregulation of banking activities, the progress made towards the completion of an integrated European financial market, financial globalisation, technological and financial innovations, the imperative of value creation and the introduction of the Euro are some of the principal forces that fuelled the process of banking consolidation in Europe.

To explain the rationale of such a movement, the economic literature mainly focused on examining the performance effects of M&A and then on its effects on competition in the underlying sector. Undoubtedly, economies of scale and scope have offered the main explanation source to performance change following M&A, leading to a number of empirical studies which aimed at examining the relationship between size and costs.

Beyond scale, scope economies and X-efficiency, revenues' diversification, risks' reduction and market power. The latter is particularly relevant in highly concentrated banking markets and when a merger or an acquisition is targeting the same activity or region.

To test these theoretical justifications, several academic studies have examined the performance change of banking M&A, using either static or dynamic analyses. The former investigates the relationship between size and efficiency and the latter assesses the changes before and after an M&A⁴. Other studies have also tried to examine the impact of M&A on market power.

The US and European main empirical findings were however disappointing. On average, banking M&A create little or no value.

A plausible explanation for the lack of significant improvement in banks' performance is that there may be other motivations such as managerial hubris or empire building by entrenched CEO.⁵ Our work especially focus on this issue, exploring two possible explanations for M&A performance. The contribution to the literature is twofold: on the one side, managerial power may influence board decisions about deals, thus influencing bank profitability. We want to test whether there is a relationship between executive power and deal performance and of what kind. On the other side, executive compensation may be used as a powerful tool to reward and incentive executives, aligning their interests to the shareholders' one and enhancing deals' performance. At our knowledge, it is the first time this issue has been studied using a sample of European domestic and cross border transactions.

After reviewing the theoretical background and the empirical findings on M&A, managerial power and executive compensation (section 2), the paper tests whether managerial power and experience of executives influences M&A performance (H1) and whether M&A performance may be seen as one of the drivers of executive compensation (H2) in section 3.⁶ The aim is to understand if any link exists among executives power, bank performance and their compensation in Europe. Our sample consists of 52 bank-to-bank M&A from EU15 countries plus Norway and Iceland. Section 4 summarizes the main results of the paper. Our conclusions are set forth in section 5.

³ ECB (2000), Ayadi and Pujals (2004, 2005), Ayadi (2007) and Figure 1 and 2.

⁴ Berger et al (1999) and Ayadi (2007).

⁵ Pilloff and Santomero (1998) and Gorton and Rosen (1995).

⁶ Masulis, Wang, and Xie (2007).

2. Theoretical and empirical backgrounds

According to the academic literature in banking and industrial economics, there is a variety of motivations driving M&A, ranging from value maximising and non value maximising value motivations.

2.1 Maximising-value explanations of M&A

The economic literature has justified banking M&A on the ground that it enhances shareholder value. Indeed, the strengthening of the shareholders' role, the increasing importance of institutional investors in banking capital (pension funds, mutual funds, private equity and hedge funds), the pressure from financial markets and new corporate governance rules have encouraged managers to orient their business objectives towards value-maximisation.

The traditional argument that M&A increase shareholder value is based on the assumption that the anticipated value of the entity created by the merger of two groups will exceed, in terms of potential wealth creation, the sum of the respective values of the two separate groups. That is: $1+1 = 3$. Two main types of synergies are achieved: operating synergies and financial synergies. The former may either be revenue enhancement or cost reduction. The latter refers to the possibility that the cost of capital may be lowered by combining one or more companies⁷.

In theory, M&A operations in the banking sector could create value by obtaining gains either in terms of efficiency or in terms of market power. An M&A allows the resulting company to obtain efficiency gains through cost reductions (or cost synergies), revenue increases (or revenue synergies), the exchange of best practices and/ or risk diversification.

Cost synergies result from an improved organisation of banking production, a better scale and/or a better combination of production factors. The core objective is to extract benefits from cost complementarities and economies of scale and scope. In practice, cost synergies might be derived from: a) the integration of different skilled teams or information technology infrastructures, b) the combination of different back-office and general services or c) the rationalisation of the domestic and/or international banking networks⁸.

Revenue synergies also derive from a better combination of production factors. Improvements in the organisation of activities, however, offer benefits from product complementarities which help to enhance revenues. In practice, revenue synergies might result from the harmonisation of product ranges, the existing complementarities between activities, cross-selling and the generalisation of a 'multi-distribution channel' approach to the various segments of customers.

It should be noted, however, that revenue synergies are much more difficult to obtain compared to cost synergies, because they depend not only on managers' decisions but also on customer behaviour. In this respect, it was estimated that some 5% to 10% of a bank's customers leave the bank after a merger.⁹ Accordingly, M&A between banking institutions in Europe have very often targeted higher cost synergies than revenue synergies (see Table 1).

In sum, efficiency gains are obtained by input and output adjustments in order to reduce costs, increase revenues and/or reduce risks so as to increase the value added. Restructuring operations can also allow efficiency gains through the reorganisation of teams (managers and

⁷ Copeland and Weston (1988).

⁸ Ayadi and Pujals (2004, 2005) and Ayadi (2006).

⁹ See Burger (2001).

employees) and/or the generalisation of 'best practices', known as 'X-efficiency' that is the managerial ability to decide on input and output in order to minimise cost (or maximise revenues).¹⁰

Lately, beyond greater economies of scale and scope, efficiency can also be improved by a greater diversification of risks (functional and/or geographical).¹¹

Efficiency may be improved following a merger or an acquisition, if the acquiring institution is more efficient *ex ante* and brings the efficiency of the target up to its own level by spreading its superior managerial expertise, policies and procedures.¹² Simulation evidence suggests that large efficiency gains are possible if the best practices of the acquirers reform the practices of inefficient targets.¹³

The M&A event itself may also improve efficiency by awakening management to the need for improvement or to implement substantial restructuring. Alternatively, efficiency may worsen because of the costs of consummating the M&A (legal and consultancy fees, severance pay and so forth) or disruptions from downsizing, difficulties in integrating corporate cultures, and in managing transition process. Efficiency may also decline because of organisational diseconomies in operating or monitoring a more complex institution.

Several studies have tried to assess the performance of M&A in banking in the 1990s. The majority have concentrated on the impact on shareholder value and efficiency. However, the results were rather mixed. The majority of empirical studies has been carried out in the United States, using a wide range of methodologies, from the most basic (event studies or balance-sheet-based indicators) to the most sophisticated (efficiency frontiers), but their findings have not been conclusive.

A large number of event studies have been carried out to assess the effects of M&A on stock market values. They all tend to evaluate the change in total market value of the acquiring company plus target institutions – adjusted for changes in overall stock market values – associated with an M&A announcement. This embodies the present value of expected future changes in terms of efficiency and market power. Although these effects cannot be disentangled, the change in market value may be viewed as an understatement of the expected efficiency improvement, since it is unlikely that an M&A would reduce the market power of the participants.¹⁴

In the US, the empirical results were mixed.¹⁵ On average, the combined shareholder value (i.e. the bidder and the target) is not affected by the announcement of the deal since the bidder

¹⁰ Originally the concept of X-inefficiency was introduced by Leibenstein (1966) who noted that, for a variety of reasons people and organisations normally work neither as hard nor as effectively as they could. In technical terms, X- efficiency refers to the deviations from the production efficient frontier that depicts the maximum attainable output for a given level of output.

¹¹ According to Méon and Weill (2001), a comparison of the annual growth rate of real GDP suggests that the economic cycles of many European countries are not perfectly correlated. Consequently, geographical diversification could enable European banks to significantly reduce their risks.

¹² Generally, the acquiring bank in a merger is more cost efficient and more profitable than the institution being acquired. As noted in a recent survey (Berger and al., 1999), this holds for the US (Berger and Humphrey, 1992; Pilloff and Santomero, 1997; Peristiani, 1997; Cummins and al., 1999 and Fried and al., 1999) as well as for Europe (Vander Vennet, 1996 and Focarelli and al., 2002). The expectation is that the more efficient and profitable acquiring bank will restructure the target institution and implement policies and procedures to improve its performance. It seems to be confirmed by the stock market performance: after a merger bidders usually lose, targets gain. The overall results is expected be positive.

¹³ Shaffer (1993).

¹⁴ Berger (2003).

¹⁵ Rhoades (1994) and Pilloff and Santomero (1997) provide a survey of event studies. Some studies of US banking M&A found increases in the combined value around the time of the M&A' announcement (Cornett and Tehranian, 1992 and Zhang, 1995); others found no improvement in combined value (Hannan and Wolken, 1989;

suffers a loss that offsets the gains of the target.¹⁶ Therefore, an M&A only implies a transfer of wealth from the shareholders of the bidder to those of the target. Compared to the 1980s, however, the evidence from the 1990s was more favourable where average abnormal returns have been higher for both bidders and targets.¹⁷

Other studies examined the stock market reaction to different types of deals. Houston and Ryngaert (1994) found that the combined gains tend to be greater when the bidding firm is unusually profitable or when there is significant overlap between institutions. The first result is consistent with a market for corporate control favouring competent over incompetent managers. The second result is consistent with the market power hypothesis, according to which a higher market share leads to higher profits. DeLong (2001) found that mergers that concentrate banks geographically or in product create value while those that diversify them don't create value.

On the other hand, Zhang (1995) found results consistent with the diversification hypothesis, according to which geographical diversification leads to a lower variability of income; and that out-of-market transactions create value for shareholders. Higher market concentration is likely to lead to an increase in prices for retail financial services, leading in turn to an increase in profits. It is also true, however, that firms operating in more concentrated markets are generally found to be less efficient.¹⁸ This effect might offset the gains from an increase in market power and thus leave unchanged the market value of the bank.

In Europe, the few studies carried out to assess the value creation through M&A in banking found positive abnormal combined returns. In the study conducted by Van Beek and Rad (1997), these returns were not statistically significant. In contrast, Cybo-Ottone and Murgia (2000) found that shareholder value gains were positive and significant, mostly driven by domestic bank-to-bank deals and diversification of banks into insurance. In 2001, Beitel and Schiereck found an increase of the combined value of bidders and targets for domestic M&A but a decrease in the case of cross-border M&A. These findings were confirmed in Beitel et al. (2004) on a sample of 98 M&A in 1985-2000, showing that transactions focussing activities and those on which targets are less performing increase value.

These positive abnormal returns, however, do not necessarily mean that mergers improve efficiency; in fact, one possible explanation for the difference between the European and American markets is that weaker antitrust enforcement in some European countries allows gains in monopoly power from in-market mergers.

Finally, it seems that the large majority of M&A undertaken in Europe or in the US, are far from having proved their effectiveness in terms of value creation in the short run.¹⁹

Houston and Ryngaert, 1994; Pilloff, 1996 and Kwan and Eisenbeis, 1999); while still others found that the measured effects depended upon the characteristics of the M&A (Houston and Ryngaert, 1997). A study of domestic and cross-border M&A involving US banks found more value created by the cross-border M&A (DeLong, 1999).

¹⁶ Stock market event studies of bank mergers have shown that merger announcements typically result in a fall in the equity value of the acquiring firm and no significant gain in the combined value of the two firms together. This result suggests that the market believes that, on average, there are unlikely to be substantial gains realised from bank mergers. And since the value of the acquiring firm typically falls, the market also believes that acquiring firms tend to overpay for acquisitions in anticipation of merger benefits that are not likely to be realised. This is a common finding and is not limited to bank mergers, which points in the direction of a more general problem associated with the corporate governance of M&A.

¹⁷ Becher (2000), Houston and al. (2001).

¹⁸ Berger and Hannan (1998).

¹⁹ According to AT Kearney (1999): "58% of the M&A announced and completed are unfortunately a failure. Indeed, the stock market value of the merged entity two years after the operation is lower than the sum of both separated partners three months before". Similarly, a KPMG survey in 2001 has shown that: "30% of the M&A have increased the shareholders' value, 39% haven't brought any considerable change and almost 31% have destroyed value". In other words, 70% of mergers were unsuccessful in producing any business benefit as regards

The empirical research based on event studies should however be taken with caution since the methodology suffers from several limitations. One problem is that the announcement of a deal mixes information concerning the proposed merger with information on its financing. Because investors consider the announcement of a stock issuance as 'bad news', the negative returns to the bidding bank could reflect the fact that mergers tend to be financed with stocks. Consistent with this notion, few studies find that returns to bidders are significantly higher when mergers are financed with cash relative to mergers financed with new equity.²⁰ Also, event studies rely heavily on investors' perception and their anticipations of the future gains when there are rumours around the transactions. This may inflict a pure speculation effect.

The studies carried out on a sample of US banks showed, on average, very little or no *cost efficiency* improvement from M&A in the 1980s.²¹ However, the results of studies using data from the 1990s were mixed.²² On the one hand, some found that mergers produce no improvement in banks' cost efficiency, especially when the deals involve very large banks.²³ It was also showed that on average, smaller banking institutions tend to exhibit larger variations in X-inefficiencies than larger institutions.²⁴ This may be due to the organisational diseconomies of operating larger firms in relation to disruptions from the M&A process, which may offset most potential efficiency gains. And on the other hand, other studies found cost reductions also for very large US banks.²⁵

The evidence for European banks is broadly consistent with the US results. Domestic mergers among banks of equal size seem to improve cost efficiency, but these results do not hold for all countries and all banks.²⁶ Nationally, studies on Italian banks or UK building societies found significant cost efficiency gains following an M&A.²⁷ Moreover, simulation evidence suggests that a cross-border acquisition may be associated with a reduction in the costs of the target, while little effect is found for domestic M&A.²⁸ On the contrary Vander Vennet (2002) found no tangible gains in terms of cost efficiency in the case of cross-border M&A. The difficulties in improving cost efficiency for domestic and cross-border transactions may be related to the obstacles often encountered, especially in continental Europe, in reducing a bank's labour force. In fact, personnel reduction, one of the main sources of savings, is hardly an option in countries with rigid labour markets.²⁹

shareholder value. Finally, according to a Merrill Lynch study in 2003, not only do most mergers fail to deliver their promised value, but large deals have tended to perform worse than smaller ones. And at least 50% of major mergers since 1990 have eroded shareholder returns.

²⁰ Houston and Ryngaert (1997).

²¹ Berger and Humphrey (1992), Srinivasan (1992) and Pilloff (1996).

²² One limitation applies to this literature, indeed, the efficiency gains or losses associated to M&A activity may take a very long period to materialise, but these studies only focus on a short period of time before and after each M&A, Berger (2003).

²³ Peristiani (1997), Berger (1998) and Rhoades (1998). Akhavein and al. (1997) and Berger (2000).

²⁴ X-inefficiencies have been broadly investigated in the US but without giving a final answer. Indeed, the first cause is linked to the size, on average, operating costs of larger banks are found to be closer to the optimal frontier curve than those of smaller banks to their respective cost frontier (Kwan and Eisenbeis (1996)). This could be explained by the fact that larger banks which operate in metropolitan markets are more likely to face stronger competition than smaller banks which are more likely to operate in suburban or rural areas. The second reason is linked to risk taking, inefficient institutions are found to take in a higher level of risk (Gorten and Rosen (1995)). It is indeed very likely that managers of inefficient banks are more inclined to compensate the operating inefficiency by taking on more risk which may reward them with a higher yield. Finally, the third reason is the financial condition which is linked to the percentage of problem loans and other illiquid positions in the balance and off balance sheets. The correlation between poor asset quality and inefficiency may be an indication of poor management.

²⁵ Houston and al. (2001).

²⁶ Vander Vennet (1996).

²⁷ Resti (1998). Haynes and Thompson (1999).

²⁸ Altunbas and al. (1997).

²⁹ Focarelli and al. (2002).

Studies on *profit efficiency* of US banks more often found gains from M&A. The fact that cost efficiency is, on average, little improved as a result of a bank merger, does not necessarily mean that there is no improvement in profits. Profit efficiency incorporates both cost as well as revenue efficiency. Revenue efficiency can be improved by simply raising prices as market power expanded through the merger process itself. Or revenues may rise because the merged institution restructures its assets mix.³⁰

Two studies in particular have attempted to determine the profit effects of mergers. Akhavein et al. (1997) found little change in cost efficiency but an improvement in profit efficiency of large US banks from 1980-90 following M&A, especially when both merger participants were relatively inefficient prior to the merger.³¹ Also, after merging, banks tended to shift their portfolios to take on more loans and fewer securities. They attribute gains in profit efficiency to the benefits of risk diversification: larger banks have more diversified loan portfolios and lower equity-asset ratios. But their measure of profit efficiency does not account for changes in risk likely to result from such a portfolio switch. Berger (1998) found similar results in a study that includes all US bank mergers, both large and small, from 1990 to 1995.

In Europe, Vander Venet (1996) found that domestic mergers of equals in European countries have a positive impact on profitability, mainly driven by improvements in operational efficiency. As regards cross-border M&A, he only found a partial profit efficiency improvement that may be caused by changes in the pricing behaviour of the acquired banks.³² Focarelli et al. (2002) found that Italian deals that consist of the purchase of a majority (but not all) of the voting shares of the target appear to result in significant improvements, mainly due to a decrease in bad loans. For full mergers, they observe that Italian banks aim to change their business focus towards providing a broader range of financial services and thus increase their non-interest income, rather than to obtain efficiency gains. After the merger, they observe an increase in profitability in the long run that is also related to a more efficient use of capital.

In practice, efficiency gains do not appear to be the only explanation for the recent M&A wave in banking. Gains obtained through increased market power seem to also offer a strong incentive to merge, but the relationship between market concentration and performance has only been verified partially.³³

Economic literature concludes that prices are positively correlated to local market shares in general, but this position may not be justified in the context of international markets (inter-banking activities, multinational companies and so forth).³⁴ Thus, value creation through market power would seem more likely to explain mergers at the local level and within the same activity (especially in retail banking), which appears to be coherent with the theoretical evidence noted above, in particular in the European Union, where the majority of the operations are within sectors and are national.³⁵

³⁰ Many studies of market structure, price conduct and profit performance found that higher bank concentration is significantly associated with lower prices for deposits, but the relationship between higher concentration and higher profits is often mixed, being sometimes significant and sometimes not. Berger and Hannan, (1998) found that cost efficiency tends to be lower in markets where concentration is higher. Indeed, higher concentration (market power) may lead to higher prices and revenues but, with less competition, the incentive to reduce costs to their minimum levels is blunted. So, the higher revenues are largely absorbed in higher costs rather than contributing fully to expanded profits. From this perspective, market concentration seems to have a greater negative effect on cost efficiency than it does on prices.

³¹ Other relevant studies include Berger (1993 and 1996), Berger and Mester (1997), Clark and Siems (1997), Cummins and al. (1999) and Berger (2000).

³² Vander Venet (2002), Arnaboldi (2004).

³³ Rhoades (1998).

³⁴ Hannan (1991) and Berger and Hannan (1989, 1997).

³⁵ Vander Venet (1996).

Nevertheless, several studies have shown that the previous correlation between concentration levels and market power diminished during the 1990s.³⁶ This could be attributed to the opening up of markets which has encouraged the entry of new competitors and thus increased the degree of contestability of the market.³⁷ Moreover, the emergence of new distribution channels such as e-banking, while contributing to the disappearance of the geographical boundaries, has made the concept of ‘local market’ less relevant.

Based on the hypothesis of the increase of market power, it appears that the creation of mega-banks, by altering effective competition, does not allow for any immediate profit for consumers because of dominant position abuses and consumers’ surplus capture.³⁸

The effects of an M&A on the collective welfare – mainly via prices – depend on numerous factors. Firstly, it is necessary to distinguish between national and cross-border M&A operations. Prior studies of the pricing effects of M&A³⁹ found that national consolidation, by strengthening the degree of concentration, could generate substantial market power, which is likely to be harmful for households and small and medium-sized enterprises (SMEs). However, the few existing studies on European bank mergers seem to conclude that there are often significant efficiency gains which result in better conditions for consumers. Huizinga et al. (2001) analysed 52 major mergers between European banks between 1994 and 1998, which were found to be largely “*socially*” beneficial. Some other studies found strong evidence of positive effects of M&A at a country level, leading to more favourable prices for consumers.⁴⁰

Conversely, cross-border M&A operations would intensify competition in the domestic market but do not change the banks’ local market shares. Consequently, the national authorities, after having encouraged the constitution of ‘national champions’, should promote cross-border and particularly pan-European operations. However, this hypothesis is relatively relaxed in view of the cross-border consolidation wave in Eastern European countries. Competitive concerns in these markets may arise if cross-border players would reach the concentration threshold perceived to be harmful to consumers.

Secondly, it is also essential to distinguish M&A operations according to the ‘means’ used – market power or efficiency gains – to create shareholder value. If the value creation occurs primarily through increased *market power*, the transaction would only constitute simple profit redistribution in favour of shareholders, but to the detriment of the customers, employees and public authorities, without a net gain in terms of collective welfare. In this case, the transaction involves a simple redistribution between the various stakeholders of the banking institution, which does not create wealth for the economy because the increase of banking profits is much lower than the welfare loss suffered by the other economic agents.

³⁶ Hannan (1997) and Radecki (1998).

³⁷ A contestable market displays low barriers to entry and exit (Baumol and al., 1982). In such a situation, potential competitors may engage in hit-and-run behaviour to take advantage of the super normal profit situation of the market. Contestability hinges on the absence of exit costs (called ‘sunk costs’), which are the costs that cannot be recovered by transferring assets to other use or by selling them. Entry to the financial services sector requires substantial investment that tends to be sunk to a high degree.

³⁸ The possibility of a cartel in banking is not purely theoretical and can be prejudicial for effective competition, as shown by the “Cruikshank” report (2000) in the UK and in the Canoy and Onderstal (2003) in the Netherlands.

³⁹ Berger and al. (1998,1999).

⁴⁰ A number of further studies exist at the country level. For example, Focarelli and Panetta (2002), by distinguishing between short-run and long-run effects of M&A, have found strong evidence that these effects are different. Precisely, they showed that national mergers leading to deposit rate changes are unfavourable to consumers in the short-run, but in the long run, if banks succeed in reducing costs, efficiency gains from mergers prevail over the market power effects, so that consumers benefit. Hence, the adverse price changes generated through consolidation are by all means temporary. Thus, studies restricted to a short post-merger period might fail to register the efficiency gains and as a consequence overestimate the adverse price changes.

Seeking other explanations for the current phenomenon, studies carried out in the United States and in Europe tend to confirm that empire building, mimicry effect and defensive reaction are factors which are likely to play an important role.

2.2. Non-maximising value explanations of M&A

When control and ownership are separated within the firm, managers can pursue other objectives than maximising shareholder value or increasing profit.⁴¹ Instead of enhancing shareholders' wealth, a manager might prefer to serve his/her own interests. Therefore, it is possible that a merger or an acquisition is simply a result of a heuristic way of addressing optimism and/or mainly dictated by the power, prestige and/or higher compensation that are related to the management of a larger firm, which is in line with the empire-building hypothesis.⁴² In that case, the desire for power is expressed, and not the direct interest of the shareholders. "Managerial power" hypothesis argues that CEOs may be able to control board decision due to their higher managerial influence. This situation is more likely to arise where shareholding is dispersed and passive.⁴³

M&A operations can also be triggered by a mimicry effect following the consolidation process initiated by competitors in the marketplace.⁴⁴ Indeed, within a relatively concentrated sector, the actions of the major 'player(s)' might have an immediate impact on the behavior of others, inducing in turn a homogeneous behavior.⁴⁵

During the last two decades, indeed, the development strategies in the banking industry were very often induced by common strategic standards, which have led to a rather homogeneous behavior. As shown in the 1980s, the commercial strategies of banking institutions were marked by a race to achieve a larger size. Similarly, in the 1990s, enhancing the profitability of shareholders' equity became the new development standard. Today, targeted value creation represents the major strategic issue in modern banking management circles.

Moreover, the acceleration of M&A operations could also result from a defensive reaction on the part of a few actors against competitors' initiatives. Indeed, as the wave of mergers spreads, banking institutions that have remained outside the process are likely to become themselves a potential target in a hostile takeover transaction. To protect themselves from possible predators, managers can pursue an active acquisition policy in order to maintain their position.

Numerous M&A carried out recently in fact seem to have been dictated by the desire to modify the existing equilibrium and to be proactive to others' actions. Sometimes disguised as a hypothetical value creation move, a number of these operations are primarily the reflection of the single market impetus, where mergers have simply become the objective rather than the result of careful strategic thinking. Most European banking institutions, reacting to the increased contestability of their national banking market, have sought to strengthen their national position, in order to improve their profitability and to protect their position from new competitive entrants.

Finally, the new mechanisms of corporate governance, including takeover threats, large and activist shareholders and effective boards, may offer a plausible explanation for the recent

⁴¹ Referred to as 'agency relation' by Jensen and Meckling (1976).

⁴² "Bidding firms infected by hubris simply pay too much for their target" (Roll, 1986, p. 1). "If there actually are no aggregate gains in takeover, the phenomenon depends on the overbearing presumption of bidders that their valuations are correct" (Roll, 1986, p. 5).

⁴³ According to 'managerial theory' (see Berle and Means, 1932; Williamson, 1964).

⁴⁴ Also called a 'follow the leader' strategy.

⁴⁵ As John Maynard Keynes once said, "worldly wisdom teaches that it is better for the reputation to fail conventionally than to succeed unconventionally".

banking consolidation process. Committed to ensuring the growth of their companies to satisfy internal pressure while maintaining their competitiveness to withstand fierce external competition and forced to provide equity capital to which pressing remuneration requirements are attached, bank managers have pursued external growth through M&A as a strategic means to expand their activities.

In our work we basically focus on non maximizing value explanations of banking M&A performance. On the one side we are interested in testing the managerial power hypothesis introduced above. On the other side we study the link between performance and executive compensation. Executive compensation has been widely studied in the literature. Much research has focused on how executive compensation schemes can help reduce agency problems in publicly listed companies. Since Coase (1937), Jensen and Meckling (1976), and Fama and Jensen (1983a, b) the contractual view of the firm has been developed and the issue of managerial power and discretion has been analysed, referring to that as an “agency problem”. The separation of ownership and control may lead to agency problems, since managers may use their discretion to benefit themselves in a variety of ways. On the other hand, shareholders, the owner of the company, delegate decisions to managers. Helland and Sykuta (2005) point out that shareholders are vulnerable to executives they cannot effectively monitor. As a part of corporate governance mechanism, executives’ hiring, firing and remuneration policies may help to alleviate the problem. In particular, compensation schemes may be used not only as a reward for past performance, but also as an incentive tool to enhance performance, to align executive and shareholder interests, and to maximize shareholders’ value.

Executives may be rewarded either in the form of cash or stock-based compensation. Jensen and Murphy (1990) and Murphy (1999) detect that cash based compensation, i.e. bonus or salary, repays past efforts but does not seem to have a clear incentive function in enhancing future performance. However, Hall and Murphy (2003) point out that stock-based compensation, like stock option or stock granting plans, better help to align executive and shareholder interests.

A comprehensive survey by Schleifer and Vishny (1997) gives the idea of the complexity of the issue. They examine the most common approaches in corporate governance, focusing on the roles of legal protection and concentrated ownership, and trying to find which system is the best. Their analysis suggests that incentive contracts may help to reduce the agency problem. Nonetheless, the major practical question in shaping a corporate governance system is how to introduce legal protection of investors.

Analysing the link between compensation and performance, it has to be mentioned that managers reward may take various forms, i.e. non-monetary remuneration. Non-monetary remuneration, such as privileges, reduced risk of dismissal, and diversification benefits, have been widely studied in the literature.⁴⁶ This form of compensation is particularly relevant in corporate restructuring, merger and acquisition. Agency problem arises and variable compensation may be used as an incentive tool linked to deals’ performance. However, in the case of a decreasing variable compensation, it may be compensated by higher non-monetary benefits, in managers’ view.

Furthermore, managers might pursue merger and acquisition to reduce their employment risk (Amihud and Lev, 1981). Shareholders may diversify their risk investing in a portfolio of shares. On the contrary, executives do not have a portfolio of employers and cannot diversify their risk on the financial markets. Risk adverse managers try to find an alternative route to diminish the employment risk. Merger and acquisition usually help to stabilize income

⁴⁶ Jensen and Meckling (1976); Jensen (1986); Jensen and Murphy (1990); Murphy (1999); Singh, Matur and Gleason (2004).

stream, thus reducing the instability of their jobs. Once more, conflicts among managers and shareholders may occur. Managers benefit from risk reduction. Shareholders may face a welfare loss due to the cost of the deal and to the possible wealth transfer to bondholders. The importance of shaping an effective corporate governance mechanism arises and manager compensation schemes play a central role. If shareholders are not satisfied with performance, they can modify executives' variable compensation. However, wage settlement cannot fully overcome the agency problem for a series of reasons, such as limitation on the monitoring activity, and stochastic optimal contract further increasing risk.

Referring to the empirical works, a first group of studies focuses on the link between compensation schemes and company performance, showing positive abnormal returns after the announcement of stock option plans adoption. Variable compensation may reduce agency problems leading to better firm results. Therefore the stock market positively reacts to such announcements. Empirical evidence support this theory since Brickley, Bhagat and Lease (1985), and Lemgruber (1986). Datta, Iskandar-Datta and Raman (2001) document a strong positive relation between acquiring managers' equity based compensation and stock price performance around and following acquisition announcements. High equity based compensation (EBC) managers pay lower acquisition premiums and acquire targets with higher growth opportunities. This indicates that, at announcement, the market views managers of high EBC firms as making better acquisitions than their counterparts in low EBC firms.

However, the above mentioned empirical evidence is not fully agreed. Tosi, Werner, Katz and Gomez-Mejia (1998) found that less than 5 percent of CEO pay appeared to be explained by performance. Barkema and Gomez-Mejia (1998) attribute the partial inability to identify a robust relationship between executive compensation and performance to many factors, such as the fact that paradigm other than agency theory have not been fully tested. Yet they mention that almost all empirical studies on CEO remuneration have used US data focusing on the US framework. Following their viewpoint, our study has a true international scope, comparing executive compensation and performance in Europe and helping to fill the void of knowledge.

Bebchuk and Fried (2003) propose an alternative approach to executive compensation and agency problem. To adequately understand the landscape of executive compensation, they suggest that the design of compensation arrangements has to be recognized as a part of the same agency problem. Managerial power affects the design of executive compensation in firms with a separation of ownership and control since managers determine the board meeting agenda and the information given to the board, especially if they are the chairman of their own boards. The existence of managerial influence over the board may be reflected in compensation schemes, such as "gratuitous goodbye payments". Core, Holthausen and Larcker (1999) show that CEOs earn greater compensation when governance structures are less effective. Besides the predicted component of compensation arising from these characteristics of board and ownership structure has a statistically significant negative relation with firm operating and stock return performance. Their result suggests that firms with weaker governance structure have greater agency problems. Greater agency problems lead to CEO's greater compensation. Finally, firm with greater agency problems perform worse.

Still considering managerial power and ownership structure, Grinstein and Hribar (2004) find that CEOs who have more power to influence board decision receive significantly larger bonus for completing M&A deals. They find a positive relationship between bonus compensation and deal performance but not between bonus compensation and deal performance. Their evidence is consistent with the argument that managerial power is the primary driver of M&A bonus.

Specifically looking at target firms, Hartzell, Ofek and Yermack (2004) study the benefits received by target CEOs in completed mergers and acquisitions. The authors find strong

inverse relationships between those benefits, which may take form of golden parachutes and payment of special cash bonuses, and the likelihood that the target CEO remains as an officer of the acquirer. The result shows that bidders overpay certain CEOs to surrender managerial control over firms' assets. Agrawal and Wackling (1994) examine the impact of acquisition attempts on the compensation of chief executives of target firms. They find that takeover bids are more frequent in industries where the chief executive has a positive abnormal compensation. Therefore the level of compensation before the bid has an influence on takeover activity related to the firm.

3. Managerial power, banking M&A performance, and executive compensation

As said in the previous paragraph, two main topics are covered in this chapter with specific reference to banking mergers and acquisitions in Europe. First we are interested in testing the managerial power hypothesis. Second we focus on the relationship between performance and executive compensation.

Executives have different level of managerial experience. Usually they increase their know-how learning by doing. In M&A deals, experience may help to better choose the target, and the timing of the deal, to exploit synergies, and to manage the transition period more effectively. If the CEO has a strong managerial power, he can influence the board to adopt the decisions he proposes. We expect that experience plays a key role, and may influence in some ways deals' performance. Therefore, under the assumption that no opportunistic behaviour is taken by the CEO, we test the following hypothesis:

H1: Does managerial power have any influence on post deal bidder bank performance?

We assess banking M&A performance using executives' experience as proxy for managerial influence. The underlying assumption is that the greater experience the CEO has, the stronger it is the influence on the board of directors. We expect to find a causality link between managerial power and bank performance. The sign of the relationship is partly due to the alignment between CEO and shareholder's interests.

Hence, a further step is to investigate whether performance of banks influences executive compensation. Our hypothesis is that variable compensation, aligning CEO and shareholder interest, may be driven by better performance. Following this viewpoint, we relate both the level and the changes in pre and post M&A performance with executive compensation.⁴⁷ We test total and variable compensation in order to check if changes occur in the results:

H2: Is there a link between executive compensation and changes in bank performance?

The circle seems then closed: stronger managerial power should lead to better deals performance. Better performance should be rewarded by higher executive compensation. This mechanism may lead to the retention of the successful CEO, further increasing his power. However other explanations may be feasible. In particular, if opportunistic behaviour takes place, stronger power does not lead to better performance, but may be linked to higher compensation.

3.1. Sample

We consider 52 completed mergers and acquisitions closed by banks headquartered in the EU15 plus Iceland and Norway from 1995 to 2006. The deals were obtained essentially from

⁴⁷ Since we consider a well specific industry, the banking industry, and geographic area, mainly characterised by the adoption of the Euro, the comparison among CEO compensation seems reasonable, even if we take the results with caution, due to differences that still characterise European countries in wage contract.

the Thomson Financial Securities, M&A SDC database. The period under scrutiny is of a particular interest because it immediately follows the regulatory changes associated with the completion of the single market programme in the EU, and it also covers the period before and after the introduction of the Euro.

All the deals included in our study are horizontal takeovers that can either be classified as complete mergers (involving the combination of the consolidating partners) or majority acquisitions exceeding the threshold of 49% of voting rights (in which the acquiring bank buys a controlling equity stake in the target bank, and both banks remain legally separate entities), in order to take into account all the operations having generated a transfer of capital control.

The targets and the acquirers are banking institutions (commercial banks, savings institutions, cooperatives banks and public credit institutions) as defined in the second banking directive. Insurance and ‘securities’ are excluded.

We collected financial data from Bankscope, a Bureau Van Dijck database, which reports, under comparable standards, information from bank annual reports. As regards executive compensation, at our knowledge no dataset is available for Europe. Empirical works have been usually based on US data.⁴⁸ Our data has been directly collected from banks balance sheets. The focus on European-specific features is a peculiar and innovative trait of our contribution.

To explore the sample, descriptive statistical analysis on the number of transactions was performed. Table C gives the number of transactions by year and country of acquirers; and Table D(a) and (b) displays the number of bidders and targets and the number of domestic and cross border transactions by country.

Most transactions are concentrated in years 1998 – 2001 (34 out of 52). This is consistent with the wave of consolidation the European banking sector has experienced during the 1990s, confirming the importance of forces such as globalisation, technical innovation, and changes in the regulation as some of the main drivers of mergers and acquisitions.

As for the country distribution of deals, Italy plays a central role in our sample. Twenty-six percent of transactions involves an Italian bank as a target or as a bidder. French banks act as acquirers in 12 percent of the sample. Generally speaking, Italy, France and Germany are countries actively involved in the consolidation process. Altogether, banks belonging to these countries act as bidder in 24 deals out of 52. This may be explained first recalling the high fragmentation of continental banking systems at the beginning of the 90s. The consolidation process has been particularly relevant in countries where deregulation incisively changed the landscape and financial system was bank-oriented. Second, among “big” European countries, Spain and the UK were involved in cross border transactions not only inside the EU15 but also with North and South American banks. By construction, our sample cannot capture the magnitude of this phenomenon, thus under-estimating the number of deals in the latter countries. Finally, among the Baltic countries, Sweden plays a key role in the consolidation process of the area (10 percent of bidders). Here the process started a couple of years later than in the continental countries, suggesting a sort of “contagion” effect, or a follow-the-leader strategy.

The sample is homogeneously distributed between domestic and cross border transactions. Forty-five banks were involved in domestic deals, 43 percent of the sample. Half of those were completed in Italy thus reflecting the consolidation process that has taken place in the Italian banking system in the last decade. In Italy, first banks looked at the internal market (1998 – 2001) and only in a second moment they moved abroad (2004-2006). Besides, in the majority of cross border transactions considered in the sample, Italian banks play the role of

⁴⁸ Compustat mainly includes data on executive compensation of US based firms.

the target. France is characterized by a similar situation, i.e. a prevalence of domestic deals, although no chronologic pattern can be identified. The situation is different in a second group of “big” European countries, such as Germany, Spain and the UK. In Germany two deals are domestic for a total of four banks involved. Cross border transactions prevail and German banks, basically playing the part of bidders, show an active role in re-shaping the European banking system. Spanish banks were both involved in domestic and cross border transactions as bidder and target with no precise pattern being identified. Finally, in the UK banks are exclusively involved in cross border transactions. The British banking system seems characterized by a higher level of contestability and lower barrier to entry, since banks act both as bidders and targets. Generally speaking, smaller countries such as Austria, Belgium, Luxemburg and the Netherlands are characterized by a higher number of cross border deals, confirming the need of going abroad to gain market shares and to enlarge the scope of activity. The Baltic countries (Norway, Iceland, Finland and Sweden) follow this trend.

Looking at the performance of transactions, the average growth of bidder ROA and ROE before and after the deal is 9 percent, whereas the average growth of cost to income ratio is almost zero. The result suggests a positive impact of deals on banks performance, especially for the profit side. On the cost side, no particular benefit seems to emerge from the M&A wave which involved Europe at the end of the '90s. This may be explained by difficulties encountered by bidders in cost cutting. For example, Italy, Germany and France, the most represented countries in the sample, are characterized by strong labour unions, which may influence executives' restructuring and synergies implementation after the deal. As for the profit, deals may easily allow to increase market shares and to cross sell products to new customers.

Turning to executive total compensation before the deal, it has been on average 5.7 million of euros. Compared to the amount of average post deal remuneration (850 million of euros), it shows a tremendous rate of growth. The result has been mainly driven by variable compensation. Incentive plans have been introduced in the late '90s in Europe, but since the beginning they have been widely adopted by the majority of banks. Nonetheless the increase of variable compensation is amazing and difficult to explain with the average increase in performance. Retention and incentive motivations may have prevailed. Such an increase may also be explained with managerial power of executives, who may be able to influence the board to get a higher compensation after a successful deal.

3.2. Methodology

In order to test our hypothesis we use OLS regression analysis on the sample described in the previous section. Concerning H1, the dependent variables are performance indicators including both profitability and cost ratios.⁴⁹

The first ones include the return on asset (ROA) which is the ratio of gross income to average assets and the return on equity (ROE) which is the ratio of gross or net income to equity. Gross income measure is preferred to net income one to avoid the differences in taxation between the European countries. ROA is a good overall indicator of a banking organization's performance that illustrates the ability of a bank to generate profits from the assets at its disposal. ROE is an alternative measure of profitability designed to reflect the return to owners' investment. It has the disadvantage that the denominator may vary substantially across banks, even those of identical size due to the mix between equity and debt capital as well as the total amount of capital held by a firm.

As for the cost side, cost to income ratio (CI) allows to examine total costs (non interest and interest expenses) to total operating revenues. This ratio reflects the ability of the bank to

⁴⁹ Rhoades (1998).

generate revenue from its expenditures. Furthermore, for many banks, revenues reflect income earned from the balance sheet as well from the off balance sheet.⁵⁰ We tested both the post transaction level and the changes between pre and post deal values of the variables.⁵¹

The independent variables used to test the impact of managerial power on bank performance are two: experience (EXPERIENC) and age (AGE) of the CEO. The first one measures the number of years the CEO has been in charge in the bank. The longer the executive has been in charge, the more information he has on the bank, and the more powerful he should be in respect to the board. The CEO should have a deeper insight in the bank strength and weaknesses, and should be able to exploit this information advantage to improve bank performance. Thus, we expect a significant positive relationship between the two variables. This can also be seen as a test for the importance of knowledge and information in a bank, which are soft skills usually difficult to assess.

In the literature age of the CEO has been considered a proxy for managerial power. The interpretation can be twofold. On the one side, the younger is the CEO, the lower is the managerial power. This may be true in some European countries, such as Italy or Germany, where the average age of board members is relatively high. However, younger CEO may be linked to better performance, since he should have a stronger motivation in increasing his prestige and power, for example compared to elder CEO close to retirement. On the other side, elder executives should be more experienced and have higher managerial power, which may lead to better performance. They should better know the industry, being more capable to influence the board. Therefore we expect a significant relationship between the two variables, but we are uncertain on the sign it might take.

Due to the scarcity of data, we are not able to test a third proxy for managerial power, the persistence of the CEO. Persistence would be computed as a dummy variable pointing out whether the CEO was still in charge after the deal or not. After a deal, the board may change. Executives with stronger managerial power may be better able to keep their position.

Thus the first equation tested takes the form of:

$$\text{PostROA} = \beta_1 + \beta_2 \text{EXPERIENC} + \beta_3 \text{AGE} + \beta_4 Y + \beta_5 \text{LSIZED} + \varepsilon$$

Referring to H2, the dependent variables are the level of CEO total and variable compensation after the deal and its rate of growth before and after the transaction. Variable compensation, is formed by stock option plans, stock granting, bonus, and pension benefits. We prefer to test total compensation too, in order to check the robustness of our results. Usually if executives do their job well, i.e. they are able to identify the best target to acquire, to manage the deal, and to exploit synergies, they should be better paid. Compensation may be used both as an incentive (variable compensation) and as a premium for good performance (fixed compensation).

Unfortunately, in this case, data taken from banks annual reports is highly fragmented. Transparency of information varies from one country to another, therefore it was not possible

⁵⁰ Among banks, derivatives are important on and off balance sheet item that may be larger as measured by notional value than total asset. Furthermore unused commitments such as credit cards, and home equity lines of credit represent major off balance sheet items that are sometimes larger in value than assets. Standby and commercial letters of credit represent an important although much smaller source of off balance sheet items for mostly larger banks. Off balance sheet activities result in expenses and also revenues.

⁵¹ These indicators refer to the bidders and analysed one year before and one year after the deal. A three-year time period would be preferable because it is more likely that gains should appear at least one year after the merger and then all gains should be realized within three years. However, the sample would suffer for a decrease in the number of observation and would be less updated.

to further split variable compensation into its parts (i.e. stock options, stock granting, bonus, pension and insurance benefits, and so forth).

In H2 the independent variables are the performance ratios, that have been already used in testing the managerial power hypothesis. The time horizon differs, since we test the rate of growth of performance before and after the transaction, and the level of performance before the deal. We expect a significant positive relationship between performance and compensation. A higher level of performance (or a higher rate of growth of performance) should lead to higher compensation. Total compensation may be seen as a reward for the past performance, thus increasing the chances to retain first-quality executives. On the other side, a higher level of variable compensation may work as an incentive for getting high future performance.

The equation tested for H2 is therefore:

$$\text{PostTC} = \beta_1 + \beta_2\text{GROA} + \beta_3\text{GCI} + \beta_4\text{Y} + \beta_5 \text{LSIZED} + \varepsilon$$

Finally, in both hypothesis testing we control for the year of the transaction (Y), for the size of the bank (LSIZED and LSIZEA) and for the type of deal (domestic or cross border).⁵² The aim is to account for the effect of M&A waves, for the dimension of the bank and for the influence of domestic issues on performance. Table E briefly describes all variables and their expected sign.

4. Results

Regarding the first hypothesis we find a significant relationship between post deal performance and the explanatory variables. First, experience, measured as the number of years bidder CEO has been in charge before the deal, is significant with a positive coefficient on average. Average executives' experience is 5 years with a maximum of 14 years. As expected, the longer the CEO has been in charge before the deal, the better he knows the bank. Information and experience on strengths and weaknesses of the bank gained working in it help to identify the most suitable target for an acquisition or a merger. It has to be added that higher experience is usually associated with stronger managerial power. In this case stronger managerial power helps to better manage a deal, to exploit synergies, and to run crucial aspects of integration process.

Second, the level of profitability after the deal is higher if the executive is younger on average. CEO age varies from 34 to 69 years old, with a sample mean equals to 55 years old. The hypothesis of a younger, more motivated CEO seems to prevail. As previously said, younger CEO would be keen to increase their power through successful deals in order to boost their career and to enhance their reputation on the long run. Again, managerial influence has a positive impact on bank performance.

The control variables are not significant, showing no particular linkage among the year of the transaction, the size of banks, the type of deal, and performance. Table F and G summarize the descriptive statistics and OLS regression results for H1.

Results are robust as for serial correlation, normality and heteroscedasticity tests and are confirmed using ROE and cost to income ratio as alternative measures of profitability and costs. In the latter case, the sign of variables is reversed, due to the fact that better performance is usually related to lower cost to income ratio. Assuming no conflicts of interest among CEO and board, younger executives who has been longer in charge seem more

⁵² The size of banks is assessed both as natural logarithm of total assets and total deposits. In particular, total deposits are taken into account in the case of ROA as measure of performance.

capable to influence board decisions thus leading the bank to higher profitability and lower costs. It has to be noticed, however, that DOMESTIC is significant with negative sign in the case that cost to income ratio is the dependent variable. Domestic deals seem more effective in keeping costs under control, thus enhancing post deal performance. This result may be explained by the fact that manager has a deeper knowledge of the regulatory, political and legislative framework, hence being more able to evaluate potential cost synergies and more effective in exploiting them.

The second step of our analysis has the aim to test if better bank performance is linked to higher post deal executive compensation. Usually, higher bank profitability should be partly used to reward the CEO for past results and incentive him to further improve performance in the future. Besides compensation may be used as a tool to retain successful CEO. The basic idea is to check if a circular linkage among managerial power, deal performance and executive compensation exist.

Unfortunately we find no link between performance and compensation, both total and variable. Compensation has been influenced only by the year of transaction with a positive sign of the coefficient. The explanation is intuitive; moving from 1995 to 2006, CEO compensation increases. Even if it might seem obvious, the result still give us some insights. First, compensation increases along time independently from bank profitability. Second, since no link has been found between performance and variable compensation, we may wonder if the latter can still be considered a good incentive tool for executives in Europe. Finally, allowing for the difficulties encountered in finding data, transparency on executive compensation is still far from being reached in Europe, marking a clear distinction from the US framework.

5. Conclusions
(to be written)

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Tables and figures

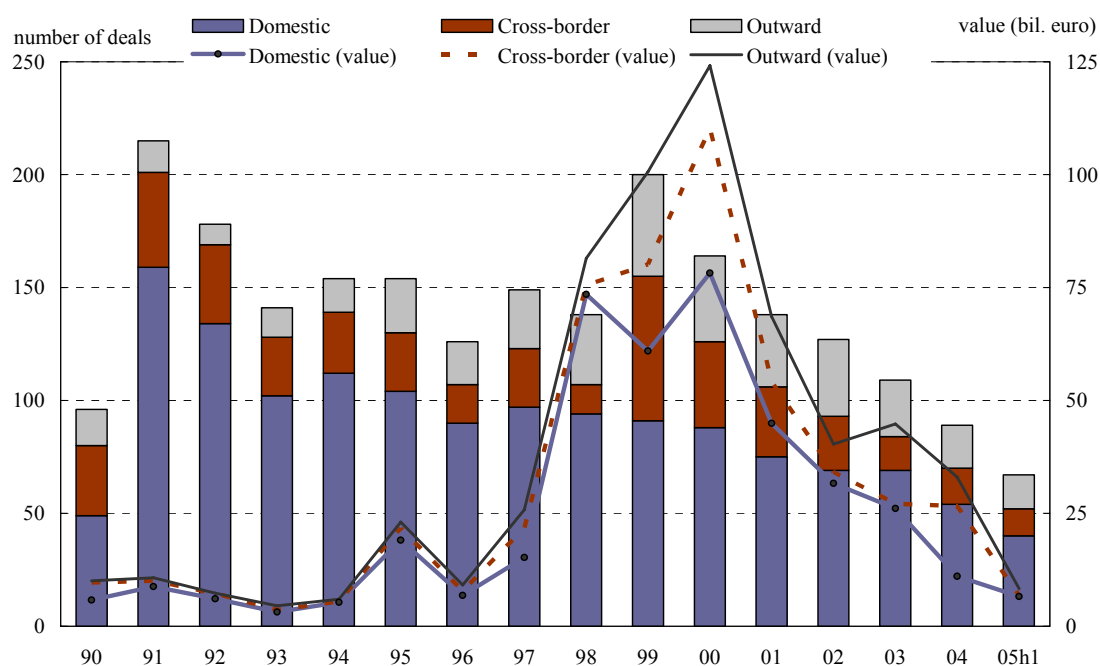
Table 1. Synergies announced in recent M&A deals in the EU

Banks	Year	Expected synergies (€ million)	Revenue synergies (%)	Cost synergies (%)
UniCredit-HVB	2005	985*	9	91
SCH-Abbey National	2004	560	20	80
Crédit Agricole-Crédit Lyonnais	2002	760	0	100
Caisses d'Épargne-CDC IXIS	2001	500	85	15
Allianz-Dresdner	2001	1080	88	12
Halifax-Bank of Scotland	2001	1113	51	49
Dexia-Artesia	2001	200	15	85
HVB-Bank Austria	2000	500	0	100
RBoS-Natwest	2000	2335	17	83
BNP-Paribas	1999	850	18	82
BBV-Argentaria	1999	511	0	100
Intesa-COMIT	1999	1000	50	50
Banco Santander-BCH	1999	630	0	100

Sources: Annual reports and financial press.

* Synergies to be achieved in 2008.

Figure 1: Number and Value of M&A in banking in EU 15



Source: Thomson Financial SDC (2006)

Note: 2005 figures are annualized. Cross-border M&A refers to transactions in EU-15 involving a non-domestic acquirer. Outward M&A refers to non-EU acquisitions of EU-15 banks (only up to 2005Q1). The number of deals is shown on the left-hand scale. Value of deals is represented as stacked lines on the right-hand scale, but is missing for a number of deals.

M&A sample:

Table C - Number of transactions by year and country of bidder

	1995	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Total	%
Belgium						3			1			4	8%
Denmark				1		1						2	4%
Finland							2					2	4%
France		1		1	1	1		1			1	6	12%
Germany	1		2	1		1		1				6	12%
Iceland									1			1	2%
Italy			4	3	3	1				1		12	23%
Luxembourg			1		1							2	4%
Netherlands		1		1							1	3	6%
Portugal					2							2	4%
Spain						1		1	2			4	8%
Sweden					2	1	2					5	10%
UK					1	1		1				3	6%
Total	1	2	7	7	10	10	4	4	4	2	1	52	
%	2%	4%	13%	13%	19%	19%	8%	8%	8%	4%	2%		

Table D(a) – Bidder and targets by country

	Bidders	Targets	Total	%
Austria	0	2	2	2%
Belgium	4	1	5	5%
Denmark	2	4	6	6%
Finland	2	1	3	3%
France	6	8	14	13%
Germany	6	2	8	8%
Greece	0	2	2	2%
Iceland	1	0	1	1%
Ireland	0	1	1	1%
Italy	12	15	27	26%
Luxembourg	2	1	3	3%
Netherlands	3	1	4	4%
Norway	0	3	3	3%
Portugal	2	4	6	6%
Spain	4	3	7	7%
Sweden	5	1	6	6%
UK	3	3	6	6%
Total			104	100%

Table D(b) Domestic and cross border transactions by country

	Domestic	Cross Border
Austria	0	2
Belgium	0	5
Denmark	2	4
Finland	0	3
France	9	5
Germany	4	4
Greece	0	2
Iceland	0	1
Ireland	0	1
Italy	22	5
Luxembourg	0	3
Netherlands	0	4
Norway	0	3
Portugal	4	2
Spain	2	5
Sweden	2	4
UK	0	6
Total	45	59
%	43%	57%

OLS analysis: framework:

Table E

Variables	Description (t = year of the deal)	Expected sign
H1		
Dependent variables		
POSTROE	Bidder ROE (t+1)	
POSTROA	Bidder ROA (t+1)	
POSTCI	Bidder Cost to income ratio (t+1)	
GROE	Rate of growth of bidder ROE = $[ROE(t+1) - ROE(t-1)] / ROE(t-1)$	
GROA	Rate of growth of bidder ROA = $[ROA(t+1) - ROA(t-1)] / ROA(t-1)$	
GCI	Rate of growth of bidder ROE = $[CI(t+1) - CI(t-1)] / CI(t-1)$	
Independent variables		
EXPERIENC	Number of years CEO has been in charge before the deal (t)	+
AGE	Age of the CEO (t)	+/-
H2		
Dependent variables		
GROWTC	Rate of growth of bidder CEO total compensation = $[TC(t+1) - TC(t-1)] / TC(t-1)$	
GROWVC	Rate of growth of bidder CEO variable compensation = $[VC(t+1) - VC(t-1)] / VC(t-1)$	
POSTC	Bidder CEO total compensation (t+1)	
POSTVC	Bidder CEO variable compensation (t+1)	
Independent variables		
GROE	Rate of growth of bidder ROE = $[ROE(t+1) - ROE(t-1)] / ROE(t-1)$	+
GROA	Rate of growth of bidder ROA = $[ROA(t+1) - ROA(t-1)] / ROA(t-1)$	+
GCI	Rate of growth of bidder ROE = $[CI(t+1) - CI(t-1)] / CI(t-1)$	+
PREROE	ROE (t-1)	+ on TC
PREROA	ROA (t-1)	+ on TC
PRECI	CI (t-1)	+ on TC
Control variables		
LSIZEA, LSIZED	Natural log of bidder total assets and deposits (t)	
Y	Year of the deal (t)	
DOMESTIC	Dummy variable : D=1 if deal is domestic; D=0 otherwise	

OLS analysis: results

Table F(a)

Variable(s)	POSTROA	EXPERIENC	AGE	LSIZED	Y
Maximum	2.49	14	69	20.7262	2006
Minimum	-0.137	1	34	12.1689	1995
Mean	0.68063	5.0288	55.4615	17.8756	
Std. Deviation	0.57159	3.0364	6.0048	1.8839	

Table F(b) - Estimated Correlation Matrix of Variables

	POSTROA	EXPERIENC	AGE	LSIZED	Y
POSTROA	1	0.16249	-0.20995	-0.13192	0.12477
EXPERIENC		1	0.43426	0.11835	-0.056938
AGE			1	0.29236	-0.066825
LSIZED				1	0.10591
Y					1

Table G - Ordinary Least Squares Estimation

Sample 1 to 52

Dependent variable: POSTROA

Regressor	Coefficient	Standard Error	T-Ratio[Prob]
C	-31.4239	69.9152	-.44946[.655]
EXPERIENC	.051587	.028244	1.8265[.044]
AGE	-.031757	.014690	-2.1619[.036]
LSIZED	-.036615	.042883	-.85383[.398]
Y	.017181	.034921	.49199[.625]
DOMESTIC	-.25872	.16649	-1.5540[.127]
R-Squared	.18800	S.E. of Regression	.54234
R-Bar-Squared	.099739	F-stat.	F(5,46) 2.1301[.079]