Consolidation Process in Polish Banking Sector – Cultural Aspects

Alina Hyz
Professor

Department of Accounting, TEI of Epirus

Abstract

This article explores merger integration processes in the Polish banking sector and the way in which the merged banks cope with difficulties emanating from firm-specific and nation-specific differences. The first part of the article analyzes mergers and acquisitions that have taken place in Poland from 1997 and attempts to measure the reaction of the capital market to the merger announcements, estimate changes in profitability and cost ratios, and investigate the development of productivity. Three factors are identified that define the significance of merger integration process: (1) the degree of compatibility of administrative practices, organizational structures and organizational cultures; (2) the kind and degree of post-merger consolidation; (3) the nature of the relationship between the two organizations. The results indicate that merged banks in Poland have increased profitability and shareholders have also experienced positive abnormal returns. However, the improvements in cost-efficiency were not so clear. Acquisitions were less successful than mergers in transferring banking practices and were probably motivated by the quest for additional market power.

Keywords: Banks; Mergers and Acquisitions; Consolidation Process, Efficiency, Cultural Aspects

JEL Classification: G21; G34

Trends in Consolidation Process in Polish Banking Sector

The financial sector since the mid-nineties has become an area of intense consolidation process. This concerned the developed countries and those who still were developing, where mergers and acquisitions involving financial entities accounted for, at the end of the twentieth century, approximately 30% of all transactions of this type carried out in Europe and the United States (DePamphilis, 2008; Cartwright, Schoenberg, 2006; Rosenbaum, Pearl, 2009). The action strategies of financial institutions often aimed at creating strong financial groups concentrated around banks. Ongoing processes of liberalization and globalization and the expansion of the European Union are contributing to increase the potential of opportunities for creating transnational companies and enterprises, mergers and acquisitions of companies.
These processes lead to the creation of international management consisting of managers of different nationalities.

The existence of cultural differences is an undeniable fact which affects the behaviour and different ways of responding to the same situations. It is therefore necessary to ask a question: whether and how the cultural diversity influences the kind of management implemented and co-operation of such groups.

The author has based his reflections on the example of the Polish banking sector, which reflects the above-mentioned processes, which Poland has begun to experience together with the acceleration of economic development in the nineties. The years 1990-91 were in Poland a favourable period for foreign investors; different measures were used for encouraging investing, but these politics faced a limited interest from investors. In the years 1992-94 National Bank of Poland was reluctant to give licenses to foreign banks, which could pose a threat to the competition of Polish banking sector. In the years 1995-1997 the National Bank of Poland subordinated giving licenses for the operation from the obligations of foreign investors to support Polish banks facing financial problems and from the participation in restructuring of the banking sector. Despite these restrictions the significant expansion of foreign capital in Polish banking sector has had occurred. On 1 January 1998 a new Act on Banking and a new Act on the National Bank of Poland came to force. The first Act introduced a minimum capital requirement at the minimum European Union level of 5 million ECU (Balcerowicz, Bratkowski, 2001). The Act obliged banks which on the day of its coming to force did not fulfil the minimum capital requirement to increase capital within two years. This requirement speeded up the growth of smaller banks and increased foreign capital involvement in the Polish banking sector, since banks with capital below the required level started to seek for foreign investors, offering them the purchase of their stock block (Kwasniak, 2000). On 1 January 1999 Poland removed restrictions applied formerly to foreign banks, concerning purchases of bigger stock blocks, opening new branches and receiving a license to establish a bank in Poland. This liberalization was a consequence of commitments undertaken by Poland when joining OECD (Sadowska – Cieslak, 1998). As a result, the environment for business in the banking sector in Poland became more competitive. We can also observe the clear benefits which result from the above discussed capital structure of Polish banking sector, the benefits include the fact that the banking system is less dependent on the State Treasury, recapitalization, restructuring, the introduction and use of modern know-how including innovations in electronic banking, investment banking and financial and investment advisory. The inflow of foreign capital is an inevitable thing as it is a component of the ongoing process of integration of the Polish economy into the world economy. (for ownership structure of Polish Banking Sector see table 1)
Table 1. Ownership Structure of Polish Banking Sector (%)

<table>
<thead>
<tr>
<th></th>
<th>1996</th>
<th>2001</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks directly owned by the State Treasury</td>
<td>28,9</td>
<td>12,4</td>
<td>11,2</td>
</tr>
<tr>
<td>Banks directly owned by National Bank of Poland</td>
<td>7,4</td>
<td>0,0</td>
<td>0,0</td>
</tr>
<tr>
<td>Other state-owned banks</td>
<td>10,3</td>
<td>2,2</td>
<td>1,8</td>
</tr>
<tr>
<td>Other domestic banks (private capital)</td>
<td>8,3</td>
<td>9,9</td>
<td>9,3</td>
</tr>
<tr>
<td>Foreign investors</td>
<td>28,1</td>
<td>58,5</td>
<td>60,5</td>
</tr>
<tr>
<td>Shareholders</td>
<td>11,3</td>
<td>12,5</td>
<td>13,0</td>
</tr>
<tr>
<td>Cooperative banks</td>
<td>5,7</td>
<td>4,5</td>
<td>4,2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100,0</strong></td>
<td><strong>100,0</strong></td>
<td><strong>100,0</strong></td>
</tr>
</tbody>
</table>

Source: Sytuacja finansowa banków w 2006 r., Synteza, NBP, Warszawa, 2007

The dominance of foreign strategic investors cause that to the Polish banking sector there are transferred the market processes which happen in a uniform European market, including the strategies of actions of international holdings and the effects of mergers and acquisitions among the strategic foreign investors.

Structure of Polish Banking Sector

Acceleration of privatization after the year 1997 led to a further decrease in state-owned banks' share in the banking sector. Their share in assets decline to 22,0%, in credits to 21,2%, in deposits to 28,9%, and in capital to 14,3%. Improvement of bank's financial situation increased foreign investors' interest in the banking sector. Foreign banks took over shares not only in state-owned banks undergoing privatization, but also in domestic private banks. In consequence of that, private banks with the majority of Polish capital have only a marginal share in the banking sector.

The years after 1997 witnessed also changes in the structure of bank's activity. The share of credits had slightly increased in assets, whereas the share of securities had decreased. Retail banking was growing fast. The share of consumption credits had increased fast in the total credits. After a period of intensified development of branches in the previous years, banks have started to concentrate on the development of new IT.

1 The Herfindahl-Hirschman Index (HHI) is defined as the sum of the squares of the market shares of the 50 largest firms (or summed over all the firms if there are fewer than 50) within the industry, where the market shares are expressed as percentages. The result is proportional to the average market share, weighted by market share. Increases in the Herfindahl index generally indicate a decrease in competition.

A $H^*$ index below 0.01 (or 100) indicates a highly competitive index.

A $H^*$ index below 0.1 (or 1,000) indicates an unconcentrated index.
Concentration of the Polish banking sector is quite low. The concentration of banking services in Poland measured by the Herfindahl-Hirschman Index (HH) is presented in table 2. In 2007 the share in the assets of five biggest banks was 46.6%, in the case of credits 44.6% and in the case of deposits 56.9% (see table 3 below).

<table>
<thead>
<tr>
<th>Year</th>
<th>Assets</th>
<th>Deposits</th>
<th>Credits (total)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>0.0792</td>
<td>0.1065</td>
<td>0.0671</td>
</tr>
<tr>
<td>2003</td>
<td>0.0753</td>
<td>0.1005</td>
<td>0.0628</td>
</tr>
<tr>
<td>2004</td>
<td>0.0692</td>
<td>0.0912</td>
<td>0.0628</td>
</tr>
<tr>
<td>2005</td>
<td>0.0650</td>
<td>0.0887</td>
<td>0.0640</td>
</tr>
<tr>
<td>2006</td>
<td>0.0599</td>
<td>0.0831</td>
<td>0.0609</td>
</tr>
</tbody>
</table>

Source: Sytuacja finansowa banków w 2006 r., Synteza, NBP, Warszawa, 2007, p. 11

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of branches</td>
<td>46.1</td>
<td>41.8</td>
<td>41.4</td>
<td>55.9</td>
<td>52.7</td>
<td>60.6</td>
<td>57.6</td>
<td>55.9</td>
<td></td>
</tr>
<tr>
<td>Number of employment</td>
<td>46.3</td>
<td>42.5</td>
<td>43.0</td>
<td>60.6</td>
<td>58.3</td>
<td>69.5</td>
<td>67.5</td>
<td>56.0</td>
<td></td>
</tr>
<tr>
<td>Share in value and dynamics of balance sheet total</td>
<td>48.6</td>
<td>46.5</td>
<td>46.6</td>
<td>69.3</td>
<td>66.7</td>
<td>64.5</td>
<td>78.2</td>
<td>76.6</td>
<td>73.9</td>
</tr>
<tr>
<td>Share in credits</td>
<td>45.0</td>
<td>44.0</td>
<td>44.6</td>
<td>63.8</td>
<td>61.7</td>
<td>60.8</td>
<td>75.6</td>
<td>75.2</td>
<td>73.3</td>
</tr>
<tr>
<td>Share in deposits</td>
<td>55.8</td>
<td>54.7</td>
<td>56.9</td>
<td>74.4</td>
<td>72.5</td>
<td>72.7</td>
<td>81.5</td>
<td>80.8</td>
<td>79.6</td>
</tr>
<tr>
<td>Share in value of share equity</td>
<td>47.5</td>
<td>45.0</td>
<td>47.9</td>
<td>67.3</td>
<td>65.7</td>
<td>65.1</td>
<td>76.2</td>
<td>76.3</td>
<td>75.5</td>
</tr>
<tr>
<td>Share in banking sector profits</td>
<td>57.2</td>
<td>54.5</td>
<td>49.6</td>
<td>75.4</td>
<td>77.6</td>
<td>65.6</td>
<td>82.9</td>
<td>86.1</td>
<td>85.2</td>
</tr>
</tbody>
</table>


As a result of consolidation processes the number of commercial banks in Poland decreased in 2007 to 64, from which 54 banks were controlled by foreign capital.

A $H^*$ index between 0.1 to 0.18 (or 1,000 to 1,800) indicates moderate concentration.
A $H^*$ index above 0.18 (above 1,800) indicates high concentration.

$^2$ Sytuacja finansowa banków w 2006 r., Synteza, NBP, Warszawa, 2007, p. 36
Institutions which invest in the Polish banking sector represent 15 countries. The value and structure of foreign core capital by country of origin can be seen in the table 4 below.

Table 4. Value and structure of foreign core capital by country of investor

<table>
<thead>
<tr>
<th>COUNTRIES</th>
<th>SHARE IN FOREIGN CORE CAPITAL</th>
<th>SHARE IN CORE CAPITAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>of which:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Belgium</td>
<td>X</td>
<td>19.9</td>
</tr>
<tr>
<td>Germany</td>
<td>14.2</td>
<td>13.4</td>
</tr>
<tr>
<td>France</td>
<td>9.6</td>
<td>7.5</td>
</tr>
<tr>
<td>USA</td>
<td>13.3</td>
<td>13.1</td>
</tr>
<tr>
<td>Netherlands</td>
<td>7.3</td>
<td>6.0</td>
</tr>
<tr>
<td>Italy</td>
<td>4.1</td>
<td>3.9</td>
</tr>
<tr>
<td>Sweden</td>
<td>X</td>
<td>2.0</td>
</tr>
<tr>
<td>Other</td>
<td>51.5</td>
<td>34.1</td>
</tr>
</tbody>
</table>


Success Factors in Mergers and Acquisitions

Companies today need to be fast growing, efficient, profitable, flexible, adaptable, future-ready and have a dominant market position. In an era of increasing globalization and competitiveness, mergers and acquisitions are considered as a strategic driver for market dominance, geographical expansion, leverage in resource and capability acquisition, competence, adjusting to competition. There seems to be a number of reasons given to merge/acquire company. These are: 1/. Coordinated Strategies - to create a number of new business opportunities and to gain competitive advantage, 2/. Scale- Purchasing companies in the same space to gain revenues, streamline cost structures, and diversify sales channels. 3/. Geographic reach- Tapping into previously inaccessible geographic markets; 4/. Customers- Acquiring companies with good customer lists. 5/. Products - Access to new products which in turn can be sold to existing customers or to reach a new customer base. 6/. Segments- Entering new vertical markets. 7/. Channels- Finding new ways of delivering the same products and services. 8/. Employees- Adding needed engineering, sales, or other talent quickly. 9/. Technology- Adding key technical capabilities or acquiring a disruptive technology. 10/. Shared Know-how - in the form of process knowledge, market knowledge and talent. Every merger, acquisition, or strategic alliance promises to create value from some kind of synergy, yet statistics show that the benefits that look so good on paper often do not materialize. The success of mergers and acquisition depends on a number of factors.
Among these one should name: 1/. Development of a strategic program of an
acquisition before its implementation, 2/. The optimal selection of a partner and accurate analysis,
3/. The appropriate evaluation of the expected synergies, 4/. The effective realization of the
connection and 5/. Establishment of a reasonable transaction price (Bertoncelj, Kovac, 2007; 
Chambers, Honeycutt, 2009; Pikula, 2008). It is reported that one of the main reasons for
failure of a merger or acquisition is based on human resources neglect. People issues have
been the most sensitive but often ignored issues in a merger and acquisition (Cartwright, 
Cooper, 1994; Wiley, 2004; Anderson, 1999)

The problems associated with the integration of companies are often underestimated
as well as problems connected with matching the merging entities in terms of strategic goals,
organizational culture, style of management etc. Seemingly similar companies may have a
different organizational culture, style of human resources management, procedures and
types of relationships between customers and employees. Until the end of the consolidation
processes the added value of the transaction is only potential. The post-transaction period
consists of an evaluation of organizational and cultural fit, strategy fit, organizational
system and cultural aspects of the merging companies. To point out the asymmetry of
information regarding the strengths and weaknesses of the company which is the object of the
acquisitions revealed in an analysis prepared by the company prior to the conclusion of the
transaction, the process of consolidation should be characterized by a high degree of flexibility
(Sudarsanam, 2003; Sudarsanam, 2002).

Mergers and acquisitions of foreign companies are much more complex than mergers
and acquisition made on a domestic market because of differences in business environment
– the subjects of a transaction of a political, economic, organizational and cultural character,
as in the field of taxation, law and accounting. All of these factors may constitute barriers in
achieving the positive effects of the transaction (Sudarsanam, 2003).

It is therefore necessary to develop a strategy of integration, especially because of the
fact that various researches confirm that among the problems associated with mergers and
acquisitions 33% are cultural and personal problems: connected with the management,
human relations, and cultures clash (Sudarsanam, 1998). The cultural aspects of an organization
understood as values, beliefs, norms, traditions can have an impact on the motivation and
effectiveness of groups of employees. One of the attempts to analyse cultures of any
organization are four cultural types (table 5.) which realize themselves through the authority,
functions, tasks, or support. The ultimate effect of transaction is affected by the degree of
cultural adaptation, i.e. integration, displacement of another culture, or keeping autonomy.
Another important factor is the influence of stress associated with changes in an
organization on a single person, its scale and duration.
Mergers and acquisitions are often associated with the fear of staff and managers of changes in their professional and private life, and this has a direct impact on involvement in the work and the implementation of a merger or acquisition. In order to overcome barriers and building mutual trust, it is important to establish contacts, especially between managers both on the ground of their professional and private life, and preserving tolerance for cultural differences.

The Role of Strategic and Cultural aspects

In this part of paper we will try to analyse the ownership structure of the Polish banking sector, taking into account the cultural aspects.

To make the consolidation process successful, it should be characterized by an adaptation of mutual structures and organizations. The two vectors of the optimization of such action are undoubtedly strategic alignment and cultural adaptation. Matrix, which gives a picture of the chance of success of international alliances, presents Figure 1.

The most beneficial are these alliances, in which both the strategic and cultural features are highly adapted to one another. This is reason why the financial and organizational analyses are not enough during the process of mergers and acquisitions. The attention should also be paid to national and organizational cultures adjustment of merging companies. It means here the ability to use the differences between two sides of the transaction and the ability of the mutual learning and openness (Bertoncelj, Kovac, 2007).

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Table 5. Types of cultural organizations

<table>
<thead>
<tr>
<th>Type of cultural organization</th>
<th>Main characteristic elements of cultural organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authority</td>
<td>The autocratic authority, critical to new challenges, emphasis on individual decision-making</td>
</tr>
<tr>
<td>Function</td>
<td>Bureaucratic function, having a hierarchy, the emphasis on formal rules and procedures, rapid assessments, and effective and standardized services providing</td>
</tr>
<tr>
<td>Tasks (achievements)</td>
<td>Tasks (achievements): flexible, emphasis on team cooperation and group decision-making, a specific task which determines the organization of work, job autonomy, requires creative environment.</td>
</tr>
<tr>
<td>Person (support)</td>
<td>Person (support): emphasis on equality, the pursuit of individual training of the various members of the organization.</td>
</tr>
</tbody>
</table>

This adjustment is a factor which has undoubtedly an impact on the success of integration in the banking sector in Poland, which manifests itself in the mental and organizational similarity between countries - investors. It is not possible to make an analysis of all the elements specific to individual nations, hence the criterion adopted was the culture of business as a combination of features of organizations and people that create them.

The five largest countries - investors in the Polish banking sector has similar characteristics. Germans, Americans, Dutch, Irish, Belgians are the nations which can be characterized by their conservatism. Also the passion for strict rules of conduct and written regulations are to a greater or lesser extent specific for each of these nations. Therefore, organizations created by them are characterized by transparent, closely hierarchized structures. Communication within the company is clearly defined and universally respected. The obvious fact is the existence of certain differences in the perception of the business environment by the representatives of particular nations (Mole, 2000). These dissimilarities are not, however, dominant in the area of professional behaviour. The examination of the countries in terms of business culture makes it even more similar.

The influence of cultural factors on achieving success in the national and international business has already been indicated. Each phase of integration will require a different set of information, but in none of them there should be a lack of knowledge of cultural differences, both in national and organizational understanding. Adequate communication and international personnel management skills become a necessity in a globalizing society.

All stages of the consolidation of an organization carry a risk arising from the obstacles encountered. They are the result of divergence of legal, organizational, and often cultural systems. Much attention is devoted to financial and organizational factors which are easy to identify and manage but forgetting about the primary barrier in each inter-human activity and all the more international communication.
Conclusions

Mergers & Acquisitions (M&A) in banking sector has become the most important strategic element driving business growth and excellence. Mergers and acquisitions will continue to be an ever-present characteristic of the modern corporate landscape. Merger and acquisition (M&A) bring together different sets of people, processes and technologies with the common objective of creating a larger, unified organization. The organization aims to benefit from the synergies of merging organisations by consolidation, rationalization and integration of the people, processes and technologies of both organizations. Human Resources (HR) and cultural aspects have the potential to play an important role during all stages of M&A. However, these issues are rarely considered until serious difficulties arise. The Human Resource dimension of M&A and cultural aspects should be accorded the same emphasis and attention given financial, legal, operational and strategic concerns. HR no longer plays a dormant role and is emerging as a strategic business partner where key initiatives undertaken such as communication, training, counseling, career planning, support workshops, building trust, coaching and compensation planning, have significant business impact. On the other side successfully integrating the two cultures of the merging companies is an essential step towards achieving a successful partnership. Both organizations, the acquiring and the acquired, will have unique and beneficial cultural elements. Rather than imposing one organization's cultural elements on the other, ‘the best of both companies can be integrated into a common culture for the new organization (Hunsaker, Coombs, 1988). This can create a win-win situation for both organizations, since it will result in a corporate culture with which both sides can identify. Defining and promoting the new corporate culture will enable employees to work together toward achieving the business goals of the new organization. Conducting a cultural audit is a useful way of obtaining useful information about the two companies’ differing cultures and helps to evaluate differences and similarities in work standards and practices. That information can raise awareness of potential difficulties and issues in the merging process, and allows the merging company to take steps to minimise culture clashes by building an effective communication structure.
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