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## **FINAL QUALIFYING PAPER**

**on the topic:**

### **Mergers and acquisitions as a means of increasing the cost of a financial institution**

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## INTRODUCTION

**Relevance of research.** In a context of constant global financial globalization, more and more financial and credit institutions are trying to increase their influence on the market. One of the ways to increase the value of your own enterprise and strengthen a competitive position is a method of mergers and acquisitions. At present, there is a common global trend to reduce the number of banking institutions in highly developed countries, which may be related, first of all, with the change in regulatory policy of state regulators to increase the requirements for activities in the banking segments of the money market.

Increased globalization and competition has led to the rise of mergers and acquisitions for firms seeking competitive advantage in their respective industries. Competitive advantage means that, the firms can extend their margins and market share worldwide.

Mergers and acquisitions have a fairly long history, but especially over the last two decades, they have become a key factor in economic development. They not only have a huge impact on all sectors of the world economy, but also facilitate the improvement of organizational structures and diversification of companies. Moreover, mergers and acquisitions lead to the emergence and development of new technologies and market segments, as well as to reduce aggregate and unit costs and to minimize risks.

Investigation of the merger and acquisition processes of the banking sector and the financial sector of the country's economy as a whole, the problem of determining the value of financial and credit institutions in the process of concluding merger and acquisition agreements devoted to the work of many domestic and foreign scientists. Among them are Campbell D., F. Reed and R. Laje, P. Gohan, D. Depamfilis, Musi Ya., Tsygan T., Pravdina N., Blank I., Gordeeva T. and others. The researches of these scientists made a flexible analysis of mergers and acquisitions in the banking sphere, the motives and effects of their implementation, factors of increasing the competitiveness of banking institutions through the implementation of such



agreements, conceptual approaches to the formation of state regulation strategies in this area.

These and other aspects of the research make this topic an incredibly topical subject. Since, for the Ukrainian banking sector, this consolidation method is the most affordable for this stage of market development and needs further refinement in order to obtain access to the international market.

**The purpose of the thesis** is to analyze theoretical principles, study methodological approaches and practical recommendations for improving the effectiveness of assessing the value of a financial and credit institution in the process of mergers and acquisitions.

To achieve the research goal, the following tasks are set:

- carry out an empirical analysis of the essence and reasons for conducting mergers and acquisition;
- analyze the mechanism of mergers and acquisitions in the banking sector;
- to substantiate the methodical bases of estimating the cost of financial and credit institution;
- to determine the tendencies of development of the banking sector of Ukraine and the competitive conditions on the domestic market of mergers and acquisitions;
- identify ways to improve the regulation of mergers and acquisitions of Ukrainian banks in the context of ensuring their competitiveness.

**The object** of the research is the processes of ensuring the growth of the value of the financial and credit institution in the process of mergers and acquisitions in the financial sector of Ukraine.

**The subject** of the study is theoretical principles, methodological approaches and practice of ensuring the increase of the financial and credit institution's value, taking into account the factor of merger and acquisition.

**Research methods.** The theoretical and methodological basis of the diploma research are the fundamental concepts of the theory of finance and banking. In carrying out research depending on specific goals and objectives, the methods of economic analysis and study of economic processes are used: monographic,

normative-calculation, index, grouping, multivariate analysis, expert evaluations, balance, sociological, system-structural, economic-mathematical modeling, and others.

**The information base of the study** is legislative and regulatory acts on the regulation of credit activities of banks; official data of the National Bank of Ukraine; analytical reviews of rating agencies Standard & Poor's, IBI-Rating, Credit-Rating; recommendations of the Basel Committee, financial reporting of banks; monographic research and scientific publications on the problem under study.

**Scientific novelty** is the proposed methodological provisions for improving the conditions for the implementation of mergers and acquisitions in the banking sector through the public disclosure of qualitative and quantitative information.

**The practical significance of the results** is determined by suggestions and recommendations for improving the regulation of merger and acquisition processes by regulators in the banking sector, based on the implementation of the experience of developed countries.

**Master's personal contribution.** The final qualifying work is an independent study by the author.

**Publications.** Separate results of the study were reflected in the scientific article: Sydorenko A. "Theoretical bases of mergers and acquisitions process in banks" // Strategies for the development of the financial market of Ukraine: Sb. sciences Art. studio Full-time study form part 2 / bp. ed. Shulga N. - K.: KNTEU, 2018 - 366 s. (C.331-335).

**Research structure.** The work consists of 3 sections, introduction, conclusions, references and appendices. The work volume is 86 pages. 12 tables, 6 figures, 5 appendices and 89 scientific sources.

## **PART I.**

### **THE THEORETICAL BASIS OF THE MERGERS AND ACQUISITIONS PROCESS IN THE BANKS.**

#### **1.1. The essence and reasons for conducting mergers and acquisitions.**

One of the most effective methods of banks development is the realization of M&A agreements. This type of agreements is one of the most widely used methods of development, which succeeds financial-lending institution that effectively work in the whole world. In the activation processes of M&A, it is very important to be properly orientated in the types of agreements executed here, and also to evaluate the basic reasons, possible consequences and their efficiency level. However, before conducting of the analysis of these processes features, it follows to concentrate on the terminological differences of the use of concepts of mergers and acquisitions.

The term "Mergers and Acquisitions" is a class of economic processes of consolidation of business and capital, which are first deployed at the microeconomic level, as a result of which large companies appear on the market instead of a few smaller ones.

The key principle behind M&A is that two companies together are more valuable than two separate companies - at least, that's the reasoning. This rationale is particularly alluring to companies when times are tough. Strong companies will act to buy other companies to create a more competitive, cost-efficient company and, theoretically, more shareholder value. Meanwhile, target companies will often agree to be purchased when they know they cannot survive.

It is difficult to define a single interpretation of mergers and acquisitions, since the process itself came from practice, and not from theory. Many scientists, even after extracting important features of M&A, draw the conclusion that, in principle, these concepts are often used as identical [6; 7; 8]. Moreover, a number of authors consider, for example, the "association" of companies" [7] as a synonym of "merger", others distinguish "merger" as subspecies of "acquisition" [9], and some



do not give a definition of term “acquisition” in general [10; 11]. In the next table are given different scientific definitions of the term “merger” ( tab.1.1).

*Table 1.1*

**Definitions of the concept of «merger»\***

Foreign authors		
1	A merger involves the full takeover by one company of another. The absorbing company retains its legal status and individuality and acquires all the assets and liabilities of the absorbing company. After the merger, the absorbing company ceases to exist as a legal entity	Bocharov V. V. [6]
2	The merger is the complete absorption of one company by another, when the absorbing company retains its name and identity, and the target company ceases to exist as an independent legal entity	Ross S. [9]
3	Merger is a union of two companies, one of which loses its brand	Van Horn J. [12]
4	Merger is a combination of two companies, in which only one of them is kept as a legal entity	DePamphilis D. [13]
5	A merger occurs when one corporation merges with another and dissolves in it	Reed F. [14]
6	In a voluntary merger, the shareholders of the company are united on a voluntary basis and divide the resources of the newly formed consolidated company, becoming the new organization's shareholders	Campbell D. [17]
Native authors		
1	Merger is the merger (mostly voluntary) of the property and the activities of several companies or the absorption of one of them by others. The capital of a new company is equal to the sum of capital of all merged companies	Goncharov S.M. [11]
2	A merger is an association of enterprises, in which at least one of them loses the status of a legal entity (usually a new legal entity is formed in the merger process). In the process of merger, companies consolidate their balance sheets. A merger is often carried out as one of the reorganization forms of the debtor company reorganization	Blank I.A. [16]

\* Note: compiled by the author by sources [6,9,11,12,13,14,16,17].

The concept of “acquisition” in most legal sources is not defined at all, whereas a large number of foreign authors use this concept as an analogue of the concept of “merger” or “unfriendly merger”. Some of these concepts are given in Table 1.2.

Table 1.2

**Definitions of the concept of "acquisition"\***

No.	Difinition	Source
1	Acquisition - taking under control one company by other	Bodie Z. [8]
2	Such a merger in which only one of the merging companies remains. In such cases, it is about acquisition	Ross S. [9]
3	Corporate acquisition is a process that assumes that stocks or assets of the corporation become the property of the buyer	Reed F. [14]
4	Acquisition is a form of merger that provides that a company that carries out an asset is a legal entity, and a firm that is taken in will be liquidated, passing all property, liabilities, debts. The company that takes in, as a result of such operation increases its assets to the amount of clean assets of the company being taken and its shareholders get the right to buy new stock shares proportionally to the proportion of participation in each. Mostly acquisition takes force .	Reisberg B.A. [15]
5	Acquisition - takeover of a holding company or other company in the form of an integral property complex (with or without the conservation status of its legal entity). Acquisition can act as one of the forms of reorganization of the enterprise. The process of absorption often has the purpose of obtaining an additional effect in the form of synergy	Blank I.A. [16]
6	Acquisition is an "unequal marriage" when one company acquires another. Under such an agreement, the absorbed company's shareholders will not become an enlarged organization's owners. Shares of a small company are redeemed by a larger company	Campbell D. [17]

\* Note: compiled by the author by sources [8,9,14,15,16,17]

Thus, the terms “merger”, “acquisition”, “takeover” are used to define the concept of “absorption” in various foreign sources. However, generally accepted is the use of the term acquisition as absorption, and "takeover" as a hostile takeover, that is, the reluctance of management by the target company.

Based on commonly accepted foreign approaches, mergers and acquisitions are part of a corporate strategy and an important component of the company's



management system associated with the process of buying, selling, dividing or merging various enterprises, helping companies to operate effectively and quickly evolve[15].

In theory, banking M&A activities could create value because of increased market power or increased efficiency, and the total value created by merger of two banks will exceed the sum of the respective values of the two separating banks.

An a merger transaction, a new company is formed by two companies. Post-merger, these separately owned firms become a single entity and are jointly owned. During the process of merger, the stocks of these companies are surrendered and the new company's stocks are issued. Generally, companies of similar sizes undergo the process of merger[1].

In Merger,  $A + B = C$

Whereas in the case of an acquisition, one company is taken over by another company and in the process, a single owner is established. Generally, a stronger and a bigger company takes over a smaller and a less powerful one. The bigger company runs the whole establishment with its identity and the smaller company has to lose its existence. In contrast to the merger, shares of the acquired company are not surrendered at all. These shares continue to be traded by the general public in the stock market[1].

In Acquisition,  $A + B = A$

A merger typically refers to a friendly deal between two firms, even if it is a complete buyout. However, an acquisition refers to an unfriendly takeover of the smaller firm, at times even unwillingly, by the stronger firm commonly heard as "Hostile Takeover". Several times a less powerful company is compelled by the bigger company to announce the transaction as a merger, even if it is an acquisition. Companies do this to avoid any negative marketing[1].

Mergers can be broadly classified into three types. They are vertical mergers, horizontal mergers, and conglomerate mergers. Let us understand each of these types hereunder:

Vertical Mergers is taking place, when a company acquires another company, which buys the products of Acquirer Company and uses them as raw material in its production process or acquires a company from which the company buys its raw material, then it is called vertical merger. If a bank acquires a marketing company which provides the bank, marketing services for its products as an outsourcing solution, then it can be stated as vertical merger;

Horizontal Mergers arise when a bank acquires another bank and merges it into itself. Similarly if a company acquires another company which is operating in the same area of its operation and merges it into itself, it is said to be horizontal merger. This could be to increase the market share, or to get technological advantages, or to enter into the new geographical areas, or to acquire any other strategic advantages;

Conglomerate Mergers happen when a company acquires a company which is not at all connected with the area of operations of acquiring company, it is said to be a conglomerate merger. For example, if a bank acquires a cement company and merges it into itself, then it can be treated as conglomerate merger. Depending upon the situation and need of the acquiring company, it may adopt any one of the above types of mergers [3].

Considering the interpretation of the concepts of mergers and acquisitions, it is possible to pass to the determination of the reasons that lead companies to realization of M&A agreements. This is some of them [18, 19, 20]:

1. Economy of scales - achieved, when charges goes down the measure of increase of the amount of rendered bank services.
2. Complementary resources. When the merger will cost more than the amount of their value before the merger, as each acquires what it lacks, and receives these resources cheaper than if they had to create them themselves.
3. Motive of monopoly and liquidation of competitors. A decisive role is the desire to achieve or strengthen its monopoly position. Sometimes competitors can be bought and then closed, because it is more profitable to buy them and eliminate price competition.

4. Complementarities in the field of innovation. The benefits of a merger can be gained due to the cost savings of high-value works in the development of new technologies and the creation of new types of products, as well as investment in new technologies and new products. One company can have good researchers, engineers, but not equipped with outsourcing capacity, network implementation. Another company may have sales channels but not innovations.

5. Available resources. The company creates large cash flows and sends balances to buy other companies.

6. Expansion of the geography of influence that will allow you to enter the new market when the opportunities of the traditional market are exhausted. In addition, becoming a multinational company reduces its propensity to local political and economic risks.

7. Eliminating inefficiencies and improving the quality of management. Mergers and acquisitions of companies may be aimed at achieving effective management, which means that one company's asset management was ineffective, and after merger its assets became more manageable.

8. Ensuring economic security and strengthening market positions. The motive of economic support helps to achieve the bank's economic development and stability, its financial and material resources protection, ability to respond adequately and without significant losses to changes in the internal and external situation.

9. Difference in the market price of the company and the cost of its replacement. It is easier to buy a current company than to build a new one. It is expedient, when the market valuations of the property complex of the company - the goals are less than the cost of replacing its assets.

10. Capital withdrawal abroad. In Ukrainian practice, the provision of safety of capital, is also characteristic of the leading of money abroad, and the screen is a merger and acquisition agreement.

11. Tax motives. High-income companies with high tax burdens can buy a tax-exempt company.



12. **Diversification.** Diversification helps diversify the bank's activities. This ensures the simultaneous development of many unrelated activities; an increase in the number of types and names of products and services; distribution of resources between different assets in order to reduce risks; penetration of the company into other industries.

13. **Decrease in financing costs (operational synergy).** For united companies, borrowing costs are cheaper than each of them individually.

14. **Personal motives of managers.** Managers can consider absorption not as a way to ensure the growth of the market value of a business, but as a means of satisfying personal ambitions, which are in the quest to lead a larger company or as a means to increase their own material well-being.

Making or inducing a company to go for an agreement with a competitor can be three groups of factors:

- the internal problem of the company, due to the need to find a new direction or mode of development;
- external conditions due to changes in the business environment, which threatens to reduce the effectiveness of the company and makes it look for new ways of development;
- their own desires, plans, and ambitions of management of the company[21].

The following main strategic reasons are the main reasons for making a decision on mergers or acquisitions:

- Elimination of a competitor. Thus, the bank gets the opportunity to strengthen its positions, increase the market share.
- Protecting your own competitive position.
- The need to strengthen weaknesses. The bank, which found that it was unable to determine the sector of maximum potential future growth and increase profitability, may find itself in a situation the best way out of which will be to search for a merger object.
- Filling the gaps. International banks can strive to combine the need to maintain their global network[28].

In general, the main reason is the obtaining of the so-called synergistic effect, ie, such interaction of uniting organizations, in which the cumulative result of the activity will exceed the total result of the activity of each of the structures. Also for the purposes of mergers and acquisitions are: growth of capitalization of the formed bank; the desire to improve the quality of management and efficiency of the bank; possibility of development of new markets; possibility of simplifying the tax burden in the sense that certain regional banks have some tax incentives; reduction of expenses and other purposes.

## 1.2. Mechanism for realization of bank mergers and acquisitions.

The M & A process is quite complex and lengthy. In general, the number of necessary preparatory procedures is very significant, and each stage of the transaction has its own peculiarities.

We propose to analyze the stages of the merger and acquisition agreement from the seller. Sell-side is one of the parties to M & A transactions whose primary purpose is the transfer of specified assets to the other party (buyer) under specified conditions. It is believed that the main objective pursued by the seller in the deal is to obtain a profit from the sale, but for different reasons, the seller's motivation may change. In the process of merger and acquisition, the seller goes through several stages, as shown in Tab.1.3. [29]

**The preparatory stage** begins with the compilation of a list of potential buyers of assets put up for sale (long-list).

The process of finding a potential buyer begins with the process of determining the characteristics of a potential buyer (investor targeting). In other words, it is necessary to determine which companies would be interested in the put up for sale asset (business).

*Table 1.3*

### The main stages of M & A transactions on the side of the seller \*

Preparatory stage	Conduct of the tender	Close the transaction
<ul style="list-style-type: none"> <li>• Preparing an asset for sale</li> <li>• Preliminary assessment of the asset put up for sale</li> <li>• Preparation of analytical materials</li> <li>• Information room filling (data-room)</li> </ul>	<ul style="list-style-type: none"> <li>• Sending a teaser - an invitation to tender</li> <li>• Receiving confirmation of interest and participation in the sales process</li> <li>• Signing up of confidentiality agreements</li> </ul>	<ul style="list-style-type: none"> <li>• Negotiation and signing of a sales contract</li> <li>• Obtaining Permits from Regulators</li> <li>• Ensuring the transfer of ownership to the buyer of assets</li> </ul>



<ul style="list-style-type: none"> <li>• Creating a list of potential business buyers</li> <li>• Preparation of non-disclosure agreements</li> </ul>	<p>Sending information memorandum to interested parties</p> <p>Obtaining indicative applications</p> <p>Definition of the shortlist of the finalists of the tender</p> <p>Data-room management and due diligence process</p> <p>Conducting presentations by road business management (road-show)</p> <p>Receiving final offers</p> <p>Negotiations with finalists</p> <p>Signing of the main terms of the M &amp; A agreement with the winner of the tender</p>	<p>Carrying out mutual settlements</p>
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\* Note: compiled by the author by sources [29].

A properly selected target group of interested buyers will depend on the performance of the subsequent business sale process. The seller must clearly understand why this buyer will be interested in acquiring the asset. The investor targeting phase completes with the list of potential buyers (long list), which will be sent teaser [30].

**Second stage** is a teaser, or investment teaser, is a summary letter that highlights the sales process and the qualities of a company for sale or an investment opportunity. Thus, the teaser is a brief information note about the company. It can be of different types: newsletter, presentation, video (which can take from 30 seconds to 1 minute and contain general information about the company, market and company's share on it, competitive advantages, etc.) [26]. The teaser is prepared by the seller (or the seller's advisor) on a no-name basis to maintain confidentiality. It is sent to prospective buyers in order to determine their initial interest in the opportunity. If the potential buyers are interested, they would then sign a non-disclosure agreement (NDA) to keep matters confidential. Following the signed NDA, more detailed

information about the company would be received, which usually comes in the form of a confidential information memorandum (CIM).

A teaser is the first contact with potential buyers, so it needs to create enough interest for the buyers to dedicate the time to pursue the acquisition further. Good teasers usually keep the potential buyers' investment criteria in mind, and they provide sufficient information and highlight the company's qualities that match this criteria.

The teaser company, as a rule, is carried out in two stages:

Stage 1 - compilation and distribution of a teaser, which should intrigue potential buyers. At the first stage of the teaser company, a circle of interested and potential investors is formed.

Stage 2 - 2-3 weeks after the appearance of the teaser comes the stage of disclosure of the object of sale to interested investors [26]. At the second stage of the binder company, an information memorandum is being sent [26].

Unlike Tizer, the information memorandum is more detailed. An information memorandum can be up to 100 pages with detailed and thorough description of the company's sales, main financial and production indicators, description of market position, competitive environment, prospects of company development, investment needs, etc. [26].

An informative memorandum is accompanied by a cover letter (process letter) in which the representative of the side sell-side offers for consideration of the potential buyer information about the object of sale and conduct of the tender. The cover letter contains a request to the buyer within a certain time (for example, two weeks) to analyze the information about the possible participation and determine the asset of interest to it [26].

The decision to continue the struggle of a potentially interesting company, the buyer must confirm the previous application indicating the indicative price. This application is sometimes referred to as a non-binding bid and is not binding in nature and legally binding on the buyer. In the future, the indicative price may be revised. On the basis of this application, the seller concludes about the seriousness of the

intentions of a buyer and draws up a shortlist of participants in the forthcoming M&A agreement [26].

The next step at this stage is a meeting between the seller and the buyers for discussing and signing the confidentiality agreement, according to which the buyer undertakes not to disclose the information about the company being put up for sale and not to disclose the information received in the due diligence process (in more detail This procedure will be considered during the analysis of the stages of the transaction on the part of the buyer, because it is he who is interested in the objective objective assessment of the company) [26].

Also, at this stage representatives of the sell-side and buy-side sign a memorandum of understanding (also known as the "letter of intent"). The memorandum of understanding contains the main parameters of the future transaction: the object, procedure and conditions of sale, the principles of price formation are determined. The protocol of intent is drawn up and signed, as a rule, in the case of one buyer. Sometimes the buy-side requires an "exclusive agreement" sign, which ensures that the seller will not negotiate with other potential buyers [26].

Before potential buyers begin to explore a potential acquisition object, the sales consultant must prepare a so-called "data-room". Previously, the information room was a room in which all the necessary documents regarding the activities of the company were collected. If there were several buyers, they were allowed in the data-room according to a certain schedule. Today, as a informational room, the virtual data-room is most often used, namely a specially created restricted access site that stores the basic documents about an M & A object [26].

On average, the due-diligence procedure lasts more than two weeks. In case of the need for clarifications, requests for documents not included in the data-room, or provision of interviews with individual employees of the company, due diligence may be delayed considerably. To accelerate the process, presentations are organized with key salesman sales managers [26].

Road-show is an external presentation for investors that is not obligatory, but is desirable in the process of business sale. Road-show is organized most often when



there are several buyers. Road-show is a long-standing business practice where M&A dealers meet and discuss many issues. Such road-show is necessary and useful both for one, and for the other party to the transaction. For sell-side it is an opportunity to see the reaction of investors to information about the company's activities and forecasts for its development, as well as explain various points of dispute. For the buy-side, the road-show provides an opportunity to see and hear those who manage the company from whom their future revenues will depend, as well as to get forecasts of development and value of business [26].

The third stage is a negotiation process. After successful completion of due diligence and road-show procedures, as well as final negotiations with companies from the short-list, the buyer's side is collecting final bids. The key point in such an application is the price, which will generally be different from the previous indicative price, since it is already based on more detailed information obtained in the due diligence process. After analyzing the received applications, the seller is determined with the final winner of the tender, with which the basic terms of the transaction will be signed, as well as the contract on deferral. The contract of deprivation - this document regulates fines in case of withdrawal from the buyer from the transaction [26].

Completion of the M & A (closing) operation can take from 2 to 12 months before all actions necessary for the final change of the owners of the company are completed. The purchase agreement prescribes the actions that must be taken before the transfer of assets to the new owner. This may be the seller's obligation to eliminate some of the deficiencies identified by the buyer, for example, such as changing the charter, settling litigation, restructuring business, if it was not carried out earlier, selling non-core assets, etc. Also, during the M & A termination period, some operational restrictions on the purchased company may be imposed, such as not to carry out operations for more than a certain amount, not to sell assets, not to dismiss top management, increase the authorized fund, etc. [26].

In the last stage of the merger and acquisition (M & A) stage, mutual settlements are conducted. At the same time it is necessary to take into account a lot

of risks, which confirmed the merger and takeovers. For example, between the signing of a sales contract, but before gaining control of an enterprise, the asset may be in a pledge, under arrest, etc. Therefore, in order to minimize risks, an optimal calculation scheme and a system of guarantees, which should be included in the contract of sale, are being processed.

Most settlement schemes are based on four schemes that include blocking for a certain period of time until the contractual terms are fulfilled or the expiry of the prescribed time period for calculations:

- blocking of funds (letters of credit, collection);
- blocking of securities or promissory notes;
- escrow account (for settlements in accordance with international law);
- third-party guarantee (banks or financial holdings).

Thus, in order to systematize the analysis, we present the main stages of the organization of a bilateral negotiation process within the framework of a standard M & A agreement in the form of Table 1.4.

Table 1.4

**The sequence of the main stages of the negotiation process within the framework of a standard M & A agreement \***

Stage	A characteristic of stage in organizing an M & A transaction
<b>Tentative contract</b>	The first acquaintance with the company through the exchange of information materials, discusses the fundamental interest of the parties and, subject to understanding, concludes a confidentiality agreement.
<b>Preliminary due diligence</b>	Estimation of benefits of future confluence by the analysis of internal information for all by the past, to the current and prognosis aspects of firm candidate, a financial model and primary estimation of cost are built on the basis of the confidential information (in safe for a candidate limits) detailed.
<b>Signing of a memorandum of intent / agreement on the takeover</b>	The primary agreement is reached on the cost of the transaction, in its structure, as well as the seller's obligation to provide access to the office documents, premises and staff of the firm-candidate of misconduct or absorption for due diligence. Signing a memorandum of intent does not oblige the parties to enter into an agreement, but only obliges them to fully contribute to the assessment of future benefits for both parties.

<b>Terminal due diligence</b>	Now everything depends on the results of the previous due diligence and differs fundamentally from it only by the degree of disclosure, which determines the value of the candidate company for M & A. According to the assessment results, the conditions stated in the memorandum of intent may change.
<b>Termination of the transaction</b>	Definition of the final price and the final structure of the transaction. There is a formal registration of all necessary documents and preliminary planning of integration.
<b>Closing an agreement</b>	Expectation of permission of regulatory bodies (in particular, antimonopoly services of the country) and intensification of cooperation between management of companies and analysts, investors, Mass media

\* Note: compiled by the author by sources [31]

Since we have completed the consideration of the merger and acquisition agreement from the seller, it will be appropriate to consider the main stages of this process from the buyer's side. Buy-side is the second party to an M & A agreement whose primary purpose is to acquire specific assets in the seller-specified conditions. Usually, buyers are privileged in the M & A deal, because they are ultimately having to pay the agreed remuneration to the seller. In fig. 1.2 shows the main stages of M & A transactions from the buyer's side [29].

The structure of a M & A transaction on the buyer's side differs from the structuring of the seller's deal primarily with the previous or, as it is called, the preparatory stage. At this stage, collecting information about the object of merger and acquisition. Usually the main source of this information is official sources, information in the media (Internet, printed media, press releases, etc.). About 70% of all financial information can be obtained from public sources. At this stage, it is appropriate to involve an external consultant who will not be linked to the seller in any way and who can provide more experienced information on the financial position of the merger and acquisition transaction object and help to objectively assess its cost, both in terms of opportunities for the buyer from the implementation of this transaction, and in terms of risks. This assessment is made on the stage of the due diligence [29].



Preliminary stage	Negotiations	Closing an agreement
<ul style="list-style-type: none"> <li>• analysis and study of market access opportunities;</li> <li>• search for potential purchasing objects and recommendations for target companies;</li> <li>• analysis of financial condition and preliminary assessment of selected potential purchasing objects.</li> </ul>	<ul style="list-style-type: none"> <li>• negotiations with owners of potential objects;</li> <li>• the organization of the purchase of investors</li> <li>• help in conducting due diligence of potential purchasing objects;</li> <li>• signing the terms of the agreement with the owners of the object of purchase.</li> </ul>	<ul style="list-style-type: none"> <li>• negotiating and signing a purchase agreement;</li> <li>• obtaining regulatory approvals;</li> <li>• mutual settlements.</li> </ul>

Fig. 1.1 The main stages of M & A transactions by the buyer\*

\* Note: compiled by the author by sources [29]

Due diligence (abbreviated as DueD and DDG abbreviations) is a pre-investment survey that allows you to obtain reliable and objective data about the business to be invested. Literally from English, this term is translated as "due diligence", "verification of due diligence", "careful observation" [29].

It is possible to distinguish the main types of due diligence:

- Marketing, the main purpose of which is to find out the current position of the company in the market. Typical research objects are the industry to which the company belongs; position of the company in the industry: segments, competitive advantages; system of distribution, conditions of relations with the main buyers; competitive strategy, risks; terms of interaction with major suppliers and contractors, relevant risks.

- Financial, the main purpose of which is to assess the company's ability to generate revenue; Identification of key financial risks. In the course of this type of audit, an analysis of assets, liabilities, profits and losses, cash flows, financial analysis (including determination of the level of profitability, liquidity, solvency).

- Legal and tax - the main purpose of this type of verification is to analyze the company's compliance with the norms of economic, labor, corporate, tax law and the definition of legal risks. Typical inspection objects are: verification of rights to the

corresponding / existing assets; verification of share rights, shares and other asset control documents; presence / absence of other property risks; assessment of tax schemes; qualification of economic relations; correctness of calculation of incomes and expenses; verification of primary documentation and tax accounting system; development of the scheme of the agreement [29].

- Operational and technological, which aims to determine the completeness and efficiency of the management system, identifying problems that may arise in the management system when changing the owner, identifying the priority measures to be taken to prevent identified risks, assessing the costs necessary for the implementation of these measures [29];

- Environmental due diligence. Many corporate agreements are associated with environmental risks. Contaminated soil, water and air, hazardous substances and wastes, claims from the public and authorities, reputational risks can be inherited by the buyer of the business when purchased from the previous owner [29].

In practice, the process of Due-Diligence is not a scholastic discipline, but rather serves as an argument in negotiating, the main purpose of which is to minimize potential risks and provide leverage to reduce transaction costs. The buyer most often comes from the fact that the seller takes the price "from the ceiling" or focuses on similar transactions that took place in the national or neighboring markets [29].

It is important to note that for both the buyer and the seller, the M & A process can be interrupted at any of the stages. The main reasons are the absence of the target companies or buyers, the discrepancy between the price expectations of the proposed price, the identification of significant barriers to the deal during the day of diligence, and the lack of consent for participation in M & A between the owners of the company [29].

Nevertheless, in order to ensure the effective application of the merger and acquisition mechanism of banks, it is advisable to adhere to a series of interrelated principles, namely: systemic; economic efficiency; cumulative; sequence; causality; purposefulness; information security; balance of profitability and risk level; creativity. Compliance by the subjects of mergers or acquisitions of banks of these

principles in practice will contribute to the effectiveness of the mechanism of their implementation, that is, will ensure full and timely receipt of their expected effects of mergers or acquisitions.



### **1.3. Methodological approaches to assessing the bank's value for mergers and acquisitions.**

The financial success of mergers and acquisitions largely depends on the net income that banks declare in the medium term (up to 10 years). Most cases of bank mergers and acquisitions have a negative short-term effect of lowering the yield per share, because the buyer's bank pays a very high merger bonus to the shareholders of another bank, resulting in the effect of EPS dilution effect [32]. In the context of this statement, the important question is raised about what income erosion can be considered significant and which is quite acceptable.

Mergers and acquisitions in the banking sector are an effective way to select effective lending institutions that can quickly adapt to the external environment and operate successfully in a competitive market environment. The combination of bank resources in the results of mergers and acquisitions gives rise to a number of advantages that allow the merged bank to obtain a certain economic effect [32].

Correct appraisal of the cost of a merger or acquisition is one of the most important conditions for successful operations of this kind. It allows partner banks to make informed decisions about the desirability of merging with other banks and the conditions for future operations [32].

Specialists in the field of valuation of business value IA Nikonova, AG Gryaznova, GI Sichov and others under the market value of an object understand the most probable price at which this object can be alienated in an open market under conditions of competition when the parties act reasonably, having all the necessary information at their disposal, and the amount of the transaction is not affected by any -what extraordinary circumstances. Allocate the following criteria for assessing market value:

- the seller is not obliged to alienate the object of evaluation, and the other party (buyer) is not obliged to accept it;
- the parties to the transaction are well informed about its subject matter and act in their interests;

- the object of evaluation is presented to the open market in the form of a public offer;
- the price of the transaction is a reasonable remuneration for the object of the transaction;
- payment for the object of evaluation is expressed in cash [32].

Thus, the main conditions under which the value of the property being sold (enterprise, bank) can be recognized as a market: access to information about the object of sale, open market and the absence of coercion in relation to the subjects of the transaction [32].

Depending on the purpose of the assessment and the circumstances, the banking institution may be valued differently. The most commonly used types of value in Ukraine are market, balancing, liquidation and investment [33].

In accordance with the National Standard No. 1 "General Principles of Appraisal of Property and Property Rights":

- market value is the value for which the alienation of an object of valuation on the market of such property on the date of valuation by agreement entered into between the buyer and the seller after conducting the relevant marketing, provided that each party acted with knowledge of the case, prudentially and without coercion ;
- balance value is costs for the acquisition of property;
- liquidation value is the value that can be obtained by selling the valuation object in a period that is significantly shorter than the exposure period of such property, during which it can be sold at a price equal to the market value;
- investment value is the cost is determined taking into account the specific conditions, requirements and purpose of investment in the object of valuation [34].

The main objective of the assessment is to calculate and justify the value of the bank as a single property complex or its separate elements - assets, liabilities, capital. Depending on the requirements of the valuers, one can identify the main goals and objectives of the bank's valuation.

Current practices in evaluating market value include several methods and techniques for assessing business, which can be divided into three main groups, or approaches: cost, comparative (market) and profitable [32].

In modern Ukrainian practice, the obligatory use of income, comparative (market) and assets approaches to the estimation of the value of any object is legally enshrined. In this case, in each of the approaches used methods of evaluation, which allow obtaining a conclusion on the value of the bank [33].

**Income approach** is based on taking into account the principles of the most efficient use and expectation, according to which the value of the object of evaluation is defined as the present value of the expected income from the most efficient use of the object of evaluation, including the income from its possible resale. The income approach is based on recalculation of the future in-flows at their current value. There are four methods of income approach (Fig. 1.2).

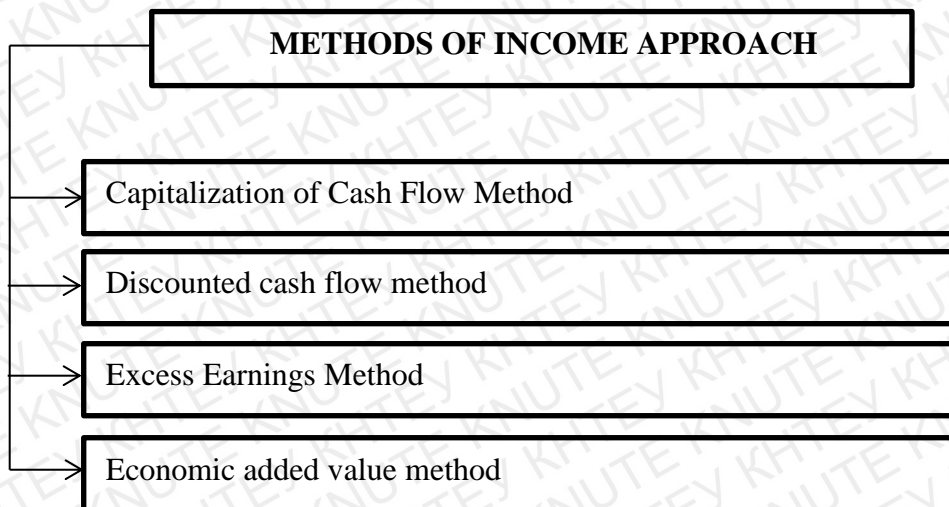


Fig.1.2. Methods of income approach\*

\* Note: compiled by the author by sources [32]

The general algorithm of calculations using a profit-based approach to valuation involves the execution of five operations:

1. Determination of future gross income.

It's evaluated:



- The potential gross income – the income that an object can bring in a year when full loading of the area before the deduction of operating expenses.

-Real gross income – based on the potential gross income from which the losses of collecting payments are deducted and added additional income from the property.

2. Deduction of operational expenses
3. Calculation and adjustment of net (operating) income.
4. Evaluation of goodwill multiplier.
5. Determine the final cost of real estate[32].

Discounting is an income-based approach to valuation that is based upon the theory that the value of a business is equal to the present value of its projected future benefits (including the present value of its terminal value).

Discounted cash flow method determines the business value by considering these inputs:

1. A stream of expected economic benefits, such as the net cash flows.
2. A discount rate which establishes the required rate of return on investment.
3. An expected gain from the disposition of the business at the conclusion of the ownership period, or the long-term (terminal) value.

The objective of the method is to determine what the expected economic benefits stream is worth in present day money, given the risks associated with owning and operating the business. Because of the method's solid financial theory foundation, it is favored by seasoned investors and business valuation professionals.

Business appraisers and economists sometimes use the formal name Discounted Future Economic Income when referring to the Discounted Cash Flow business valuation method.

The use of this method involves determining the forecast period, the frequency of revenue generation and making a forecast of future cash flows and bringing them to their present value by discounting. This method evaluates one of the most

fundamental characteristics of the bank - the ability to generate cash flows and takes into account the time factor of the value of future cash flows [36].

Therefore, it is considered the most acceptable, it helps to most clearly reflect the forecast of the development of the institution for the future owner. After all, the object of purchase ultimately is not a set of assets, which traditionally include fixed assets and intangible assets, and the flow of future income, which allows the investor to predict the payback period of investment and obtaining a certain profit. Here is a formula (1.1) for discounting cash flows:

$$Value = \sum_{t=1}^{i-n} \frac{CF_t}{(1+r)^t} \quad (1.1)$$

Where: Value - the value of the bank;

$CF_t$  - net cash flow in a certain period;

r - discount rate;

n - the life of the asset [36].

It is important to note that when applying the method of discounting cash flow to assess the value of a bank is the most important is the correct determination of the discount rate. The discount rate is the interest rate used to calculate and bring future cash flows into a single value of current value, which is the basis for determining the market value of the bank within the framework of the income approach [36]. If we consider the discount rate on the economic position, then it can be defined as the value of the capital attracted by the bank.

The main methods of determining the discount rate are:

- CAMP (equity valuation method capital),
- WACC (Weighted Average Cost of Capital),
- cumulative method
- determination method discount rates based on profitability
- expert method
- normative method
- method of determination of the rate discounting based on market multipliers.

But practically, the most commonly used only two of mentioned methods: CAMP and WACC.

To calculate WACC, one multiplies the cost of equity by the % of equity in the company's capital structure, and adds to it the cost of debt multiplied by the % of debt on the company's structure. Because interest in debt is a pre-tax expense, the cost of debt is reduced by the tax rate (it's effectively tax deductible).

The formula is

$$WACC = \frac{V_e}{V_e + V_d} \times K_e + \frac{V_d}{V_e + V_d} \times K_d \times (1 - T) \quad (1.2)$$

Where:  $K_e$  - the cost of equity.

$K_d$  - cost of debt.

$T$  - corporate tax rate

$V_e$  - value of equity

$V_d$  - value of debt

CAPM is that investors need to be compensated in two ways: time value of money and risk. The time value of money is represented by the risk-free ( $r_f$ ) rate in the formula and compensates the investors for placing money in any investment over a period of time. The risk-free rate is customarily the yield on government bonds.

The other half of the CAPM formula represents risk and calculates the amount of compensation the investor needs for taking on additional risk. This is calculated by taking a risk measure (beta) that compares the returns of the asset to the market over a period of time and to the market premium. The formula is:

$$k_e = R_f + \beta (k_m - R_f) + S_1 + S_2 + C \quad (1.3)$$

Where:  $R_f$  - Risk free rate;

$\beta$  - the beta coefficient;

$k_m$  - expected return on equity the market;

$S_1$  - size premium;

$S_2$  - risk premium;

$C$  - country risk premium [36].



The coefficient  $\beta$  in the world practice is calculated by specialized firms by analyzing the statistical information of the stock market. These results are published in periodicals that analyze stock markets. Professional appraisers, as a rule, do not deal with calculations of coefficients  $\beta$  [36].

In international practice, the risk-free rate of return is the yield rate on long-term government debt obligations. In domestic banks, it is appropriate to accept the official rate of refinancing as a non-risky rate [36].

It is important to calculate this model for taking into account the premium for the country's risk, which reflects the additional income that the investor will require for the risk associated with investments in the Ukrainian economy compared with the economy of the most developed countries, for example, the USA [36].

Thus, an estimation of the market value of a bank using the method of discounting cash flows can only be performed if certain conditions are fulfilled. First, the use of this method is justified only if the bank operates on the market for quite a long time and its activity is stable and predictable. Because the cost of the bank is based on future, not on past cash flows [36].

Capitalization method is acceptable in the case of a number of conditions. The main thing is that the bank should receive levels of profits over a period of time. However, such a situation in the banking sector is extremely rare, as the modern economy develops with a certain cyclicity. There are a number of varieties of this method, based on the capitalization base. In particular, distinguish capitalization [37]:

- net profit after taxes;
- profit before tax;
- the amount of actually paid dividends;
- potential dividends, etc.

In order to assess the bank's value, the capitalization method uses the capitalization method based on the discount rate. In order to obtain a capitalization rate, it is necessary to reduce the discount rate by the value of average annual growth rates of income [36].

It is worth noting that this method is usually used to correct previous estimates of value. And use it as the only method of estimating value is not appropriate, since the reliability of such an assessment will be low. This is due to the fact that the method does not take into account the value of assets that are in the property, namely, the residual (liquidation) value of the bank is not taken into account [36].

The method of capitalization of incomes provides for the use of gross and net approaches. For a net approach, the value of a bank is defined as the ratio of net profit to the rate of capitalization. In the gross approach, the cost of a bank is set as the difference between the share from the dividing of profit to paying interest and the amount of loan capital to the weighted average cost of capital [37].

An important prerequisite for using the method of discounting cash flow or indirect capitalization is effective and stable market activity over a long period of time and profit. An important feature of the method of discounting cash flows is that the assessment of this method takes into account time and risk factors, market conditions [36].

One of the most promising modern developments in the theory of cost estimation is the Model Olson (Edwards-Bell-Ohlson valuation model, EBO model). It allows you to take advantage of income and property approaches, to some extent, minimizing their disadvantages. According to this model, the value of a company is expressed in terms of the current value of its net assets and discounted flow of "over" - income (deviations of profit from "normal", that is, the average industry size). Formally, the model of Olson makes it possible to determine the value of the bank based on the following indicators: the book value in recent years, which is calculated on the basis of market data, discount rates, the amount of paid dividends, as well as two empirical parameters, the values of which are established according to the data of the entire market.

Features of accounting by Ukrainian banks are characterized by the fact that the value of assets indicated in it does not correspond to the market. In practice, domestic valuation experts use an unadjusted accounting value, which leads to an inadequate estimate of the bank's value.

**The asset approach** is sometimes referred to as a valuation based on the assets of the bank. The main purpose of using this method is to assess the value of assets under the hypothetical condition of selling the bank [38]. In this approach, the following basic methods (Fig. 1.3).

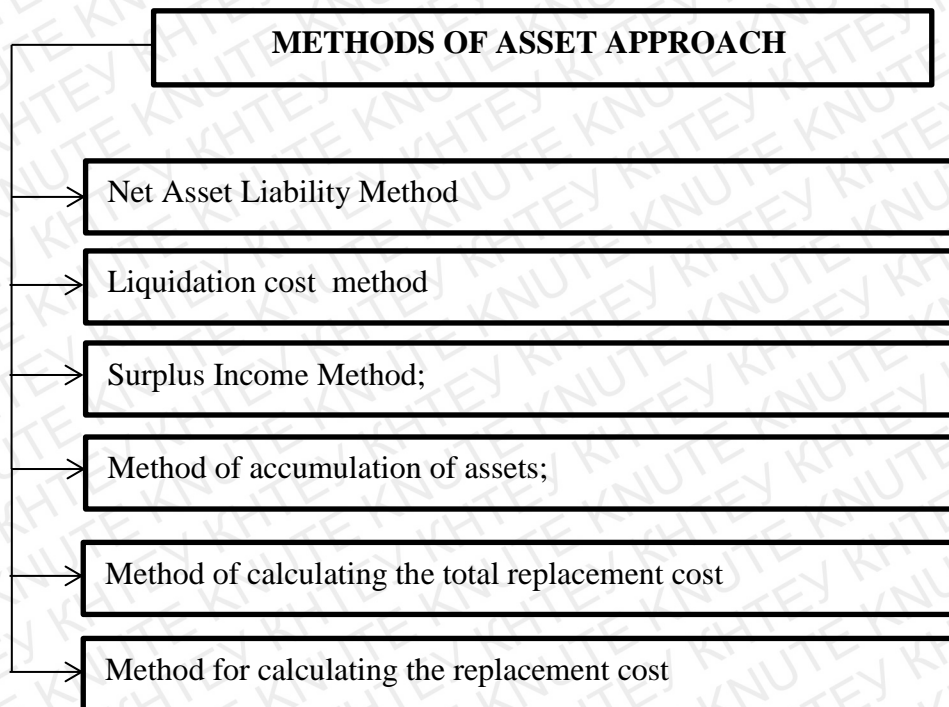


Fig.1.3. Methods of asset approach\*

\* Note: compiled by the author by sources [32]

The asset approach begins by creating a financial picture of the company through information on the balance sheet. Current asset values may differ dramatically from the assets' acquisition costs. Although the balance sheet lists assets and liabilities at historical cost, accurately using this method depends on recasting those costs and capturing the current value.

An important procedure in any business valuation is to define the business ownership interest subject to valuation. The assignment should specify whether the analysis intends to conclude a defined value for the subject company:

- total assets,
- total long-term interest-bearing debt and total owners' equity,
- total owners' equity, or



- one particular class of owners' equity.

Each of these descriptions is a valid objective of a business valuation. And, each conclusion is often referred to as a "business value." However, each of these business value conclusions will be quantitatively different for the same company. Each of these business value conclusions will be appropriate in the right circumstance - usually based on the actual or hypothetical transaction that is being analyzed.

The Asset-based Approach is based on the principle that the value of the equity of a company is equal to: the value of the company total assets minus the value of the company total liabilities

If properly applied, this valuation formula can be used to indicate the value of any of the valuation objectives listed above. However, there are two foundational words in the above formula: value and total.

The Asset-based Approach is based on the value of (and not the recorded balance of) the subject company's assets and liabilities. The standard of value in the analysis has to be defined. The valuation date of the analysis has to be defined. The standard of value is determined by the assignment. Common standards of value for taxation and accounting purposes include fair market value and fair value. Other common standards of value include investment value, owner value, use value, user value, and others. Whatever the assignment-specific standard of value is, the value conclusion is likely going to be different from the recorded account balances presented on the company's balance sheet.

Some analysts believe that the Asset-based Approach is only applicable to so-called asset-intensive companies. This conclusion is technically correct. However, this conclusion ignores the reality that virtually every company is an asset-intensive company. The fact is that the Asset-based Approach is applicable to tangible-asset-intensive companies - and to intangible-asset-intensive companies. Virtually all companies are either tangible-asset-intensive or intangible-asset-intensive (or a combination of both asset types). Therefore, the Asset-based Approach is applicable to most types of companies.

Some analysts also believe that the Asset-based Approach is only applicable to so-called asset holding companies. In fact, this approach is applicable to any company that owns assets. So, the Asset-based Approach may apply in the valuation of asset holding companies, and it may apply in the valuation of asset operating companies. Just about every company falls into one (or both) of these two categories. Therefore, for analysts who know how to perform asset valuations on a going-concern premise of value basis, the Asset-based Approach is applicable to most types of companies.

This method has a number of disadvantages, which are primarily due to its simplicity and universality, but is often used in the practice of assessing the value of banks in Ukraine. However, it should be noted that this method is not adapted for use in assessing a certain share of the bank, and it isn't recommended to take it as a basis, since the book value does not rarely adequately reflect the value of banks [36].

The cost approach is characterized by determining the amount of costs necessary to restore or replace the object of evaluation, taking into account its deterioration. The essence of this approach lies in the elemental assessment of the market value of assets and liabilities of the bank, which is compared with the corresponding value of their book value. An important condition for applying this approach to cost estimation is the availability of internal information. And its absence makes it impossible to use this approach [36].

In this regard, there is also a simplified approach to the application of this method for assessing the market value of banks, in particular, in terms of net assets, take the amount of equity or regulatory capital, which is the market value of the bank. However, as the practice of valuing the bank shows, equity, and even more so regulatory, is less than its market value several times [36].

Another method of cost approach is a method of disposal value. Liquidation value is the value of an object of valuation in the event that the object of evaluation is to be alienated in a period that is less than the usual term of exploitation of similar objects [34].

Liquidation value can be determined: at liquidation of the bank, financing of bank reorganization or reorganization of the bank [36].

**A comparative approach** to determining the market value of a bank includes methods based on data on merger and acquisition transactions. Their essence consists in a comparative analysis of the main parameters of the activity of analogous banks with the evaluated bank, namely, the values of equity and assets, the level of profitability and risk, and the market value as a benchmark is accordingly partially adjusted [36]. Main methods of this approach are listed below (Fig. 1.4.)

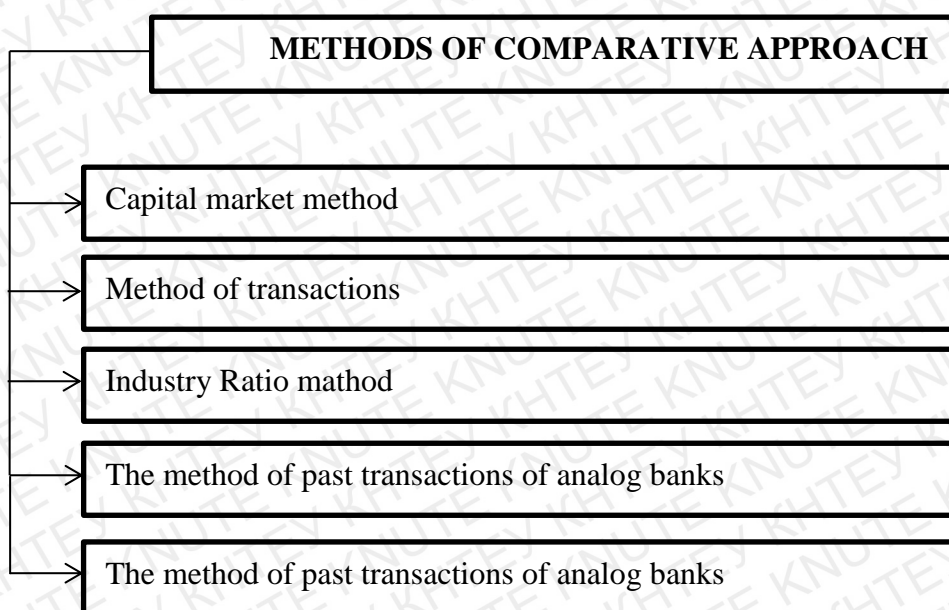


Fig.1.4. Methods of comparative approach\*

\* Note: compiled by the author by sources [32]

The comparative approach to valuing the bank includes the following methods for determining the value of: the market capital method, the analogue bank method and the sectoral coefficients method [36].

One of the main conditions for using the analogue bank method is the data on the sale and purchase of comparative objects. However, as we have already seen, the banks that became the object of sale differ in many parameters. That is why the final result of the valuation needs to be adjusted, given the number of differences between



analog banks. Consequently, difficulties in the process of evaluating the value of this method arise at the following stages [36]:

- Collecting the necessary information - unfortunately, data about the price of the transaction are not always publicly disclosed, usually the data is presented approximate;
- Comparison of a list of similar banks, in particular, it should be noted that it is very difficult to form groups of similar parameters and performance indicators, and at the same time, that the transaction took place in a time interval before the valuation date; the size in this situation is the most important criterion for drawing up the final list of analogues;
- Introducing final corrections that eliminate differences in bank parameters [36].

This method is used under certain conditions. Namely: analogue banks should be sold in a period close to the assessment of the bank's value, which should be evaluated; there should also be no speculative transfer of ownership rights, and analogue banks can not be absorbed by other banks, since the price in in such a case does not reflect the real value. Analog banks should be similar to the main financial indicators, namely: the size of the bank (income, number of staff, value of assets); assortment of offered operations and services; technological and technical equipment; level of risk and capital value; receiving regulatory requirements of the NBU, etc.

If there is a discrepancy between the specified parameters of analogue banks, it is more expedient to use multipliers, in particular:

- the cost of the bank / capital;
- bank value / profit;
- asset value / cost of the bank;
- bank value / cash flow, etc. [36].

The method of market capital is widely used in countries with developed stock markets and a significant share of bank shares in listing stock exchanges. In domestic conditions, this method is inappropriate to use. The possibility of conducting analogies with mergers and acquisitions in the United States, Japan, or the United

Kingdom is inappropriate, since information on transactions between banks that could be used as a basis for comparison may distort the real value of a Ukrainian bank, while the development of a modern stock market does not allow this method to be applied. [36].

The method of sector coefficients involves calculating the bank's value using the local business activity index, which is used as a coefficient. This ratio is based on data from similar companies that have been sold recently. Different sectors have different coefficients.

However, this is a simplistic method of valuation that does not provide an adequate assessment of the bank's value, because it does not take into account the features of the valuation object and does not take into account the characteristics of each individual bank [36].

The use of cost multipliers involves the use of data on the value of banks, which is determined as a result of an agreement on the sale and purchase of a block of shares of the bank-analogue.

Market value based on the multipliers of value within the framework of the comparative approach is determined by the formula:

$$\text{Value} = k * X, \quad (1.4)$$

Where: k - is the multiplier;

X - the corresponding indicator of the bank activity;

Value - the cost of the bank [36].

However, an expert score is also characterized by a certain level of subjectivity, which may result in insufficient accuracy of the calculations.

When applying the analogue banks method, the actual selling prices of similar banks are used as a benchmark for valuing value. The price is taken for the base (for example, for shares), which is set by the market, and adjustments are made. This method is based on retro information and, therefore, reflects the actual results achieved by the bank. In addition, the comparative approach, as well as cost, does not take into account the prospects of the bank's development, as it involves the use of retrospective data.

The study of the advantages and disadvantages of these methodological approaches, which are depicted in Table. 1.8, showed that existing approaches do not fully meet the need for information on the cost of a bank, the management of the bank and its management, because due to lack of openness do not provide complete information on the formation of value [36].

The study of existing methodological approaches and methods for assessing the value of an enterprise allows us to conclude that it is impossible to use none of them as a base and that it is expedient to use several methods in assessing business, while the real value of a company is in the range between the maximum and the lowest of the estimates. The advantages and disadvantages of each method are given in the table 1.5.

*Table 1.5*

**Advantages and disadvantages of evaluation methods\***

<b>Approach</b>	<b>Provided opportunities ("advantages")</b>	<b>Limitations of applicability ("disadvantages")</b>
<b>Asset approach</b>	<ol style="list-style-type: none"> <li>1. Provides the ability to fully identify the specific assets owned by the company.</li> <li>2. Allows allocation in the algorithm of specific elements of wear and obsolete.</li> <li>3. Takes into account the current and long-term debt.</li> <li>4. You can use it to evaluate new objects and objects that do not create a flow of income.</li> <li>5. Allows you to calculate the company's liquidation value</li> </ol>	<ol style="list-style-type: none"> <li>1. Much depends from company accounting policies and valuation of fixed assets.</li> <li>2. Does not reflect the income-generating potential of the company.</li> <li>3. Not fully able to take into account all aspects of economic obsolete</li> </ol>
<b>Comparative approach</b>	<ol style="list-style-type: none"> <li>1. The most reliable indicator of the market.</li> <li>2. Reflects the general view of financial investors in the industry in the short and medium term.</li> </ol>	<ol style="list-style-type: none"> <li>1. Demands the presence of an active market to select the required number of comparable transactions.</li> <li>2. Has limited application in conditions of low liquidity in the whole stock market.</li> </ol>



<p><b>Income approach</b></p>	<ol style="list-style-type: none"> <li>1. Reflects the logic of most business decisions.</li> <li>2. Takes into account the income-generating potential of the company.</li> <li>3. Takes into account the time factor.</li> <li>4. Takes into account the risks associated with both the industry and the enterprise itself.</li> <li>5. The best way to measure total wear and obsolete.</li> <li>6. Because of its specificity, it fully takes into account economic obsolete</li> </ol>	<ol style="list-style-type: none"> <li>1. The level of speculation (analysis and abstraction) is high</li> </ol>
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\* Note: compiled by the author by sources[7]

Consequently, all approaches to evaluating the bank's value are rather complex due to objective and subjective factors (forecast data, individuality and specificity of each bank, completeness of information) [36].

From the analyzed methods, the methods of comparative and income approaches, in particular the method of valuation using cost multipliers and discounting of cash flows, most realistically reflect the process of formation of value. After all, when assessing the value of the comparative approach used data banks analogues, taking into account the peculiarities of the formation of the value of banks in Ukraine. As international comparisons in this case are incorrect due to different conditions of cost formation (demand, foreign economic situation, transparency). However, there are also factors that do not contribute to a qualitative assessment. First and foremost, this is an ineffective market for corporate control, as well as generally unreliable or completely lacking information on negotiations and the results of sales transactions. According to Western experts, in 90% of cases, the method of

valuation is used within the limits of the income approach. Such an assessment makes it possible to determine its possible development prospects, which is the most significant advantage over other methods given above. Therefore, an income approach, as a rule, is one of the effective methodological approaches to assessing the value of a bank.

## **PART II.**

### **INVESTIGATION OF MERGERS AND ACQUISITIONS OF DOMESTIC BANKS.**

#### **2.1. Stages of the merger and acquisition process in Ukraine.**

In the Ukrainian legal acts that regulating banking activities, there is no law that describes the mechanism for the implementation of the merger and acquisition process, but some of them this process described as a way of reorganization the bank, in particular:

1. Law of Ukraine “About Banks and Banking” describes the reorganization of the bank as a process of merger, joining, selection, division of the bank, the transformation of its organizational legal form, the consequence of which is the transfer, acceptance of its property, funds, rights and duties to legal successors [2].

2. Law of Ukraine “About simplification of bank reorganization and capitalization procedures” determines that the Bank or banks have the right to reorganize by joining another bank [3].

There is no separate takeover statute in Ukraine. The main laws and regulations that govern various aspects of business combinations, including takeovers, in Ukraine are as follows:

- the Commercial Code of Ukraine of 16 January 2003;
- the Civil Code of Ukraine of 16 January 2003;
- the Law of Ukraine ‘On Companies’ of 19 September 1991;
- the Law of Ukraine ‘On Joint-Stock Companies’ of 17 September 2008;
- the Law of Ukraine ‘On Protection of Economic Competition’ of 11 January 2001;
- the Law of Ukraine ‘On State Registration of Legal Entities, Private Entrepreneurs and Non-governmental Organisations’ of 15 May 2003;
- the Law of Ukraine ‘On Securities and Stock Market’ of 23 February 2006;
- the Law of Ukraine ‘On Regime of Foreign Investments’ of 19 March 1996;



- the Law of Ukraine ‘On Re-establishment of Debtor’s Solvency or Declaring it Bankrupt’ of 14 May 1992; and
- the Labour Code of Ukraine of 10 December 1975.

Ukrainian law sets specific rules for M&A in the banking and financial sectors.

As regards banks, any reorganisation process (including merger) within a bank in Ukraine shall be approved by the NBU. The latter also approves the plan of such business reorganisation. If someone intends to acquire or increase a substantial shareholding in a Ukrainian bank (10 and more per cent of the charter capital or voting rights), this person must obtain consent from the NBU.

It is also required to obtain the relevant approval for acquiring or increasing a substantial shareholding (10, 25, 50 and 75 per cent of the charter capital or voting rights) in other financial institutions that provide certain financial services, eg, insurance companies, leasing companies, investments funds, etc. A potential investor is obliged to obtain a written consent from the National Commission for the Regulation of Financial Services Markets.

**Companies Register.** Information on merger (amalgamation, absorption), change in charter capital or, for limited liability companies (LLCs), participant structure must be filed with the Ukrainian Companies Register. In this case, the fees depend on the type of filing, whether it is registration of changes or a newly established legal entity. However, the registration fees are insignificant and usually are around €20.

Ukrainian laws provide for restricted regulation on tender offers or exchange offers. In particular, conditions to a tender offer are statutorily limited to the following: in JSCs (whether public or private) the shareholder who acquired more than 50 per cent of the shares (directly or indirectly) is obliged to make a public offer to the remaining minority shareholders to buy out their shares at a price of no less than the market value. Such public offer shall be made within 20 calendar days from the date of acquiring the controlling shareholding, and the minority shareholders may exercise their right to sell the shares within the period from 30 to 120 calendar days. The public offer is irrevocable and binding, and the majority shareholder is obliged

within the specified period to buy out the shares of minority shareholders who accepted the offer. In such a case, financing may not be conditional. In other cases, financing in a cash acquisition may be made conditional; eg, the availability of financing may be a condition precedent a share-purchase agreement.

Other forms of business combination in relation to unlisted companies, save for the exception with the private JSC as mentioned above, may be contingent on any condition the parties may agree apart from cases when such agreements contradict the principles of good faith according to the Civil Code of Ukraine. The most common conditions are obtaining corporate approvals or merger clearance from the national competition authority or clearance from the authorised state bodies in regulated areas (financial, insurance, etc).

Reorganization of banks in Ukraine is carried out in several stages: preparatory stage; implementation of measures envisaged by the plan of reorganization; completion of reorganization (appendices A)

The preparatory phase includes: obtaining a permit from the National Bank for reorganization and making a decision on reorganization (if the reorganization of the bank is carried out by the decision of its owners); decision-making by the National Bank on the forced reorganization of a bank in the event of a significant threat to the solvency of a bank, provided that there is a proposal by another bank to join or merge with this bank; adoption and agreement with the National Bank of the decision on compulsory reorganization (if reorganization of the bank is carried out by the decision of the interim administration). At the same time, the plan for reorganization of the bank is approved at the preparatory stage.

In the second stage, in accordance with the bank reorganization plan, the following measures are envisaged: obtaining the holders of substantial participation in the bank by written permission of the National Bank for the acquisition or increase of substantial participation in the successor bank; inventory and valuation of assets and liabilities of the bank; drawing up of a transfer act (in the case of reorganization through merger, accession or transformation) or distributive balance (in case of

reorganization by division or allocation); approval of the transfer act or balance of payments.

At the stage of completion of the reorganization of the bank it is envisaged: entering into the State register of banks the exclusion of the reorganized bank; entering into the State Register of Banks a record of the registration of the successor bank.

The methods and procedures for reorganizing banks may be different, but the assessment of possible financial results and the control of these processes is entrusted to the National Bank of Ukraine.

In the Resolution of the National Bank of Ukraine No. 189 of June 27, 2008 (with amendments and supplements) "On Approval of the Regulation on the Peculiarities of the Bank's Reorganization by the Decision of its Owners", the procedure for passing the stages for the reorganization procedure is determined:

- 1) preparing and providing materials to the participants of the reorganized bank, such as an explanation of the terms of the merger agreement (merger) or division plan (separation, transformation).
- 2) the adoption by the supervisory (supervisory) board of each merging bank, the decision to approve the draft agreement on the merger of banks, approval of explanations to the terms of the merger agreement;
- 3) obtaining the supervisory (supervisory) board of the reorganized bank, the conclusion of an independent expert on the terms of the merger agreement (if necessary);
- 4) adoption by the general meeting of each participating bank of a merger, a decision on reorganization of the bank, which should contain the information provided for in Article 28 of the Law of Ukraine "On Banks and Banking Activities" and on approval of the merger agreement;
- 5) after adoption by the general meeting of the bank participants of the decision on the reorganization of the bank submission to the National Bank of documents for obtaining a resolution of the National Bank for the reorganization of the bank and approval of the National Bank of the reorganization plan;



6) after obtaining the permission of the National Bank to conduct a reorganization of submission of documents to the state registrar for inclusion in the Unified State Register of a record regarding the decision of the participants of the bank on the reorganization of the bank in accordance with the requirements of the Law of Ukraine "On State Registration of Legal Entities and Individual Entrepreneurs";

7) a written notification of the bank's lenders and the publication in the official printed body of a notice of reorganization of the bank by merger;

8) satisfaction of claims of creditors, declared to the bank being reorganized, in accordance with Article 82 of the Company Law;

9) the sale by the shareholders of the bank of the right to demand mandatory redemption of securities belonging to them in the manner prescribed by Articles 68, 69 of the Companies Act;

10) approval by the National Bank of the acquisition or increase of a substantial participant's participation in the successor bank;

11) commission by the commission for the reorganization of the transfer act;

12) the adoption by the supervisory (supervisory) board of each bank participating in the reorganization, the decision to approve the draft statute of the bank created by the merger, the approval of the transfer act prepared by the commission for the reorganization, as well as the approval of the conditions for the conversion of shares of the bank, which terminated in the shares of the successor bank;

13) acceptance by the general meeting of each bank participating in the merger, the decision on approval of the transfer act, the charter of the successor bank, and also about the election of the authorized persons of the bank for further actions concerning the banks being reorganized;

14) submission by authorized representatives of banks - participants of the reorganization of the application and all necessary documents for registration of the issue of shares to the National Commission on Securities and Stock Market;

- 15) registration by the National Commission of Securities and Stock Market of the issue of shares and issuance of a temporary certificate on the registration of the issue of shares;
- 16) assignment of shares to the international identification number of securities;
- 17) conclusion of a contract with the depository on servicing the issue of shares;
- 18) exchange of shares (shares) of the bank created by the merger, on the shares (units) of the banks being reorganized;
- 19) approval of the results of placement (exchange) of shares (shares) by the authorized banks of banks - participants in the reorganization;
- 20) submission by the successor bank to the National Bank of the documents necessary for the approval of the charter;
- 21) state registration of the charter of the successor bank by the state registrar;
- 22) submitting to the National Commission on Securities and Stock Market a report on the results of the placement (exchange) of shares;
- 23) registration by the National Commission of Securities and Stock Market of the report on the results of the placement (exchange) of shares created as a result of the merger of the bank and the cancellation by the National Commission of Securities and Stock Market of the registration of shares issued by the banks being reorganized;
- 24) the submission by the successor bank to the National Bank of documents for obtaining a banking license, a general license for foreign exchange transactions, permits (if necessary), and making information to the State Register of Banks on the registration of the successor bank;
- 25) submitting by the successor bank to the National Bank of documents for opening a correspondent account of the bank;

26) submission by the bank, which was reorganized through a merger, to the National Bank of documents for recording in the State Register of Banks about the termination of the bank and all its separate units as a result of the merger;

27) state registration of the termination of a legal entity as a result of the merger;

28) obtaining a certificate of state registration of the issue of shares of the successor bank.

The main objective of this Resolution is to accelerate and accelerate M&A processes. The main problems raised by this document are: an economically unjustified approach to determining the conversion factor, preparing an independent expert's opinion, providing shareholders with merger documents, disclosing information in the process of merger, differentiating the powers of the reorganization commission and the executive body. Thus, the NBU proposes to divide the procedures of simplified capitalization and reorganization, simplify the process of reorganizing banks only by joining, create an opportunity for a simplified reorganization only for:

a) banks in need of an additional capitalization - Large banks on a regular basis procedure;

b) banks with a transparent ownership structure - Exclude investor participation.

At the present stage of development, Ukraine is increasingly taking part in the integration processes of the world economy, this movement necessitates the study of consolidation processes in the banking sector of Ukraine as one of the ways to improve the reliability of the domestic banking system, ensuring its development, and not stagnation during the financial crises as at the state level, and in the world as a whole.



## **2.2. Analysis of mergers and acquisitions of banks in Ukraine.**

Basically, there are three common ways of business combinations in Ukraine. The respective legal schemes may be classified as follows:

- statutory mergers,
- share purchases; and
- asset acquisitions (which also includes a specific for Ukraine - purchase of an integrated property complex).

Ukrainian laws envisage two main forms of mergers: amalgamation and absorption. Amalgamation is a merger of two or more companies into a new company. Under amalgamation, the merging legal entities cease to legally exist, whereas all their property and liabilities are transferred to a newly established company. Merger by absorption occurs when the undertaking, property and liabilities of one or more companies are transferred to another existing company that is the only one surviving the merger.

Given the complexities and long-lasting procedures associated with statutory mergers in Ukraine, the most common scheme for business combinations are takeovers through share purchases. Such share purchases may take a form of direct purchase of shares in the Ukrainian target company or, as is quite often the case, through a purchase of shares in the offshore companies holding control over such Ukrainian target company.

Under Ukrainian law, it is also quite common for business combinations to be structured through acquisition of the target's particular assets. In addition, Ukrainian law envisages a specific possibility to acquire the target company integrated property complex - a specific form of real estate common in post-Soviet jurisdictions that usually includes buildings, facilities, equipment and related liabilities.

The last two decades can be characterized without exaggeration by significant changes for the financial world. This trend can be traced through the removal of geographical and economic boundaries, which was reflected in the increase in cash

flows in the global economy. Accumulation of a large mass of cash has led to an increase in the concentration of bank capital in developed countries.

The tendency to increase capitalization on the domestic market is evidenced by events that actively contributed to the process of capitalization of domestic banks. The first precondition for this was the adoption by the National Bank of Ukraine on August 6, 2014, of a resolution No.464 "On bringing the authorized capital of banks to the minimum size". According to this document, by June 17, 2016, banks should raise the minimum amount of authorized capital up to UAH 120 million, and in 2024 it should be at least UAH 500 million [44].

Thus, according to the decision of the National Bank of August 6, 2014, from the middle of 2016 the minimum amount of the authorized capital of the bank will increase annually according to the following schedule:

- 120 million UAH until June 17, 2016;
- 200 million UAH - until July 11, 2017;
- 300 million UAH - until July 11, 2018;
- 400 million UAH - until July 11, 2019;
- 450 million UAH - until July 11, 2020;
- 500 million UAH - until July 11, 2024.

At the same time, all new (created) banks are required to have a minimum authorized capital of 500 million hryvnia. Previously, this strap was set at UAH 120 million [44].

The given normative document has led to a sharp reduction of the number of commercial banks during 2014-2018 ( Figure 2.1).

As can be seen from the chart above, the number of commercial banks in Ukraine decreased more than twice (for 100 institutions) during 2014-2018, the most dramatic decline will be in 2016, compared with 2015, 46 institutions from the domestic market "came out", thus the market was shrinking by 28%. This can be explained by the entry into force of the first stage of increasing the requirements for the minimum amount of authorized capital, which was not able to reach a number of banks, and were forced to cease their activities.

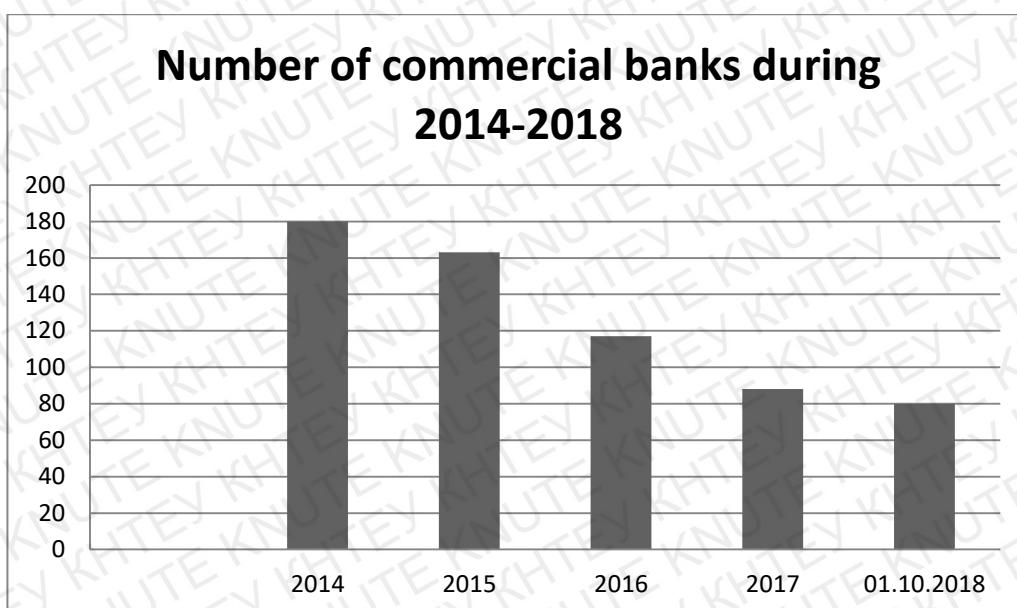


Fig. 2.1 Dynamics of the number of commercial banks during 2014-2018

\* Note: compiled by the author by sources[45]

A further study of the dynamics of the development of the banking sector in Ukraine in recent years suggests that, according to macroeconomic criteria, it has gained prominent positions.

In addition, the banking sector of Ukraine actively implements the recommendations of the Basel Committee on Banking Supervision, which characterizes its readiness to meet international criteria and requirements [43].

During 2006-2017 there were several waves of changes in the dynamics of quantitative and qualitative indicators of the functioning of the banking sector of Ukraine, which created conditions for active action in the market of mergers and acquisitions in this area. The growth of the basic macroeconomic parameters of the banking sector during 2006-2009 changed their decline in 2010-2017, and the tendency of restoration of the banking sector in 2013 was suspended due to the transition of the country's economy to actually military conditions of operation. At the same time, the banking sector was one of the first to react negatively to external threats [77]. However, even with the current instability in the banking sector in 2015-2016, its macroeconomic parameters are now significantly higher than ten years ago. The highest level of bank assets in Ukraine's GDP (Gross Domestic Product) was recorded in 2008-2009, when it was 97.7-93.6% of GDP, respectively. One of the



single articles of the banking sector that grew in 2017, compared with 2016, is the authorized capital of commercial banks, which amounted to 17.3% of Ukraine's GDP, compared to 9.9% in the previous year, which is directly related to the requirements the regulator to the minimum capital, which was already discussed above [47] (Table 2.1).

*Table 2.1*

**Dynamics of key indicators of the banking sector of Ukraine in% to GDP for 2007-2017\***

<i>Indexes</i>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
<i>Regulatory capital</i>		10	13	14,9	14,9	13,7	12,7	14,1	12,1	6,6	5,4
<i>Assets</i>	62,5	83,2	97,7	95,6	87	81	80	87,8	84,1	61,6	50,9
<i>Equity</i>	7,8	9,7	12,6	13,2	12,7	11,9	12,1	13,2	9,4	4,7	5,0
<i>Share capital</i>	4,8	5,9	8,7	13	13,5	13,2	12,5	12,7	11,5	9,9	17,3
<i>Loans and customer due diligence</i>	45,1	59,2	77,4	79,2	67,7	61,6	57,9	62,6	65,1	37,8	41,8
<i>Obligation</i>	54,7	73,5	85,1	85,2	74,3	69	67,9	74,6	74,6	56,9	45,9

\* Note: compiled by the author by sources [48,50]

The ratio of loans to GDP in 2016 amounted to 37.8% and in 2017 increased to 41.8%. The ratio of own capital to GDP increased from 4.7% to 5.0 %% in 2016 - 2017. A similar trend and dynamics occurred with the ratio of the authorized capital of banking institutions to GDP, it also experienced an increase from 9.9% to 17.3% in 2016-2017 [48].

The formation of the competitiveness of banking institutions depended on capital build-up, asset quality improvement, deposit policy, and the ability to provide profitability. The regulatory capital of banks in 2008 - 2017 increased almost three times (by 266%) to UAH 109.7 billion. in 2017, which was 5.4% of GDP. At the same time, the growing needs of the real sector of Ukraine and the strengthening of international competition require an increase in the level of capitalization of banks and their concentration on an even higher level [48].

The liabilities of banks for 2008 - 2017 increased by 139% and at the beginning of 2018 reached UAH 1,093.8 billion. Among them, individuals 'funds

grew at a significant pace - to UAH 425.5 billion, which was almost 40% of the banks' liabilities. Funds played a key role in increasing the resource base of banking institutions. Loss of confidence in banking institutions in the conditions of rapid bankruptcy of both small and systemic banks of the first group causes the reduction of an important source of financing of banks - funds of the population. This increases the risk for banks and implements the policy of limiting the solvency of the population and currency instability [47].

The total assets of banks during the period of 2007 - 2017 increased by 3.5 times and in 2018 amounted to UAH 1 212.8 billion. Livest share of loans granted by banking institutions (82.1%), which during the period of 2006 - 2017 increased by 4 times (to UAH 996.2 billion as of 01.01.2018) [47].

These trends have prompted the market to address the issue of increasing capitalization of banks, and the most widespread method of concentration of capital used in the domestic money market is the merger and acquisition agreements, which became the main manifestation of financial globalization. This process is directly related to the accelerated pace of development, which led to significant deviations in the level of capitalization of the financial services industry in different countries.

Thus, these and other conditions encourage the state to closely monitor the mergers and acquisitions of companies, not only by increasing its role in these processes, but also by changing the legal framework governing the respective field of activity. Against the backdrop of an increase in the level of interest in M & A deals, they can gradually acquire a political color, which usually does not entail an increase in the efficiency of their implementation. In addition, transnational mergers and acquisitions play an important role in these transactions, as they are an integral part of the country's market development. This, in turn, leads to a conflict of interest between private capital of foreign financial institutions and the national business, where each party wants to maximize its profit to meet its own goals [52]. Thus, all players in this market can be divided into two camps [53]:



- those who actively use the market for mergers and acquisitions to achieve their goals: initiates transactions, forms a strategic business model, that is, generators of mergers and acquisitions;
- those who are hostage to external conditions and not at their own will fall into the epicenter of this process, which the market forces to transform and modify, not only to become a strong competitor in the market, but also to not lose its advantages over other players.

It is worth noting that M & A is influenced both by external and internal factors that are determined by the specific business of a certain company by companies and the approach to choosing a M & A strategy.

The internal prerequisites that lead the financial institution to decide on the possibility of selling or buying another company depends, first of all, on the goals and objectives that it sets itself in the process of establishing a long-term strategy of operation. This may be a desire to expand the boundaries of their business (that is, an increase in the network of branches, that is, an increase in their geographical boundaries, or the desire to consolidate themselves in the local market through the expansion of product policy), the need to change the organizational form in order to enter the international markets, etc. [54].

The market for mergers and acquisitions in Ukraine in the first half of 2018 is slowing down. According to the M & A Ukraine, 11 agreements have been concluded and 22 contracts are under negotiation. These figures are significantly lower compared to the corresponding period of 2017, when 29 agreements were concluded. The financial sector continues to dominate the number of M & A transactions in Ukraine - it accounts for 33% of total transactions and 33% of total deals in 2016-2017.

In September 2017, TAS Group acquired Sberbank's VS Bank for USD16 million. Elsewhere, the banking and insurance sector saw higher levels of deal activity but with a lower level of invested funds. In 2016, Unicredit's USD323 million sale of UkrSotsbank to Alfa Group, accounted for 43 percent of the total deal value in the country. In 2017 a total of 14 deals were announced with a combined



value of USD40 million, driven mainly by the sale of Ukrainian subsidiaries of Russian banks due to limitations imposed by the National Bank of Ukraine (NBU) in March 2017. As a result of the NBU's limitations, which include a ban on dividend distribution and repayments of intrabank loans abroad, most Russian banks operating in Ukraine have either already exited or are in the process of doing so.

Concluding from the development of the M & A market in the banking sector of Ukraine, one can distinguish its features:

- most transactions - takeover or rehabilitation;
- low degree of transparency and openness of transactions; – strong dependence on the actions of the regulator;
- consolidation with the aim of developing a network of branches, attracting new clients of geographical presence or diversification;
- absorption by banks with the state participation of troubled banks for the purpose of sanitation to avoid their collapse, which can lead to severe consequences of a social nature and cause instability of the financial sector of the economy.

Today, the overwhelming majority of M&A transactions in the banking sector of Ukraine is the nature of the acquisition by a large foreign bank of a medium-sized or small domestic regional bank. Often, the purpose of such acquisition is either expansion of the client base or geographic penetration. In this case, we can not talk about any significant changes in the structure of the industry, which can affect the state of the banking system as a whole. This type of transaction can not be considered an effective tool for solving existing problems in the industry. Here we should talk about the mergers and acquisitions of medium and small banks, as a result of which they not only increase their capital base, but will also be able to compete with large private and state banks. To do this, it is necessary to stimulate transactions, first of all, from the state by facilitating the procedure for their implementation, pursuing a rigorous policy regarding minimum capital requirements, transparency of their operations, and the owners of the bank.

Note that during 2005-2010, mergers and acquisitions in the banking system of Ukraine took place mainly with the participation of foreign banks, or rather, the account of the absorption of Ukrainian banks by foreign ones [60].

The peculiarity of the development of the M & A market in the banking sector in 2011 was that it was this year that clearly observed operations aimed at the concentration of the domestic banking market. And according to experts' forecasts in the future there will be a significant reduction in the number of banking institutions in the market of banking services. This trend also poses a threat to the financial security of banking institutions as a result of possible market monopolization [60].

The high activity of mergers and acquisitions has always been observed in the banking sector of Ukraine. The peculiarity of Ukraine is that all M & A deals in the banking sector were implemented using only cash payment form. This is explained, above all, by the fact that "banks-buyers" significantly outperformed the assets of "target banks" [60].

A precondition for today's revival of such processes is the emergence in the market of more "buyers" of this specific product, which is explained by a certain stabilization of the economic situation after the financial crisis. Prices for Ukrainian assets have increased, which prompts owners to sell them [71].

In 2012, significant changes took place in the banking sector of Ukraine - seven of the well-known European financial institutions left our market. According to expert estimates, at least two more banks are planning to sell their Ukrainian divisions. The sale of assets is due to crisis processes in Europe, as well as internal problems in the Ukrainian market, in particular the slowdown in economic growth, lower than the expected profitability of the banking system, high level of problem debts and expectations of devaluation of hryvnia in Ukraine [71].

The buyers are mainly Ukrainian and Russian financial institutions. Thus, "Erste Group" sold its "Erste Bank" to the owner of "Fedobank". At the end of 2012 Russian "Sberbank" acquired the Austrian "Volksbank" and the merger of Ukrainian units of these banks began (Table 2.2). Unlike most banks, Sberbank actively expanded its loan portfolio and opened new branches [71].

Table 2.2

**Dynamics of M & A transactions during 2012-2017\***

№	Date	Seller	Buyer	Buyer's Country	Price	Subject of the transaction,% of shares
1	30.07.12	Bank Forum	Смарт-Холдинг	Ukraine	92 mln USD	96,06
2	19.11.12	Credit Agricole corporate & investment bank	Credit Agricole	Ukraine	-	100
3	01.04.13	Swedbank	Delta Bank	Ukraine	175 mln USD	99,9
4	04.13	Erste Bank	Fidobank	Ukraine	83 mln USD	100
5	08.13	Brokbusinessbank	East European Fuel and Energy Company (SEEPEK)	Ukraine	100 mln USD	80,00
6	18.07.13	Astra Bank	Delta Bank	Ukraine	120 mln USD	100
7	01.14	Pravex-Bank	Group DF (Dmitry Firtash)	Ukraine	100 mln USD	100
8	01.14	Bank of Cyprus	Alfa Bank	Russia	276 млн USD	100
9	01.14	Marfin Bank	Delta Bank	Ukraine	20 mln USD	100
10	02.14	Bank Avangard	Investment Capital Ukraine (ICU)	Cyprus	-	100
11	08.14	Universal Bank	Delta Bank	Ukraine	125 mln USD	100
12	12.14	PrivatBank Georgia	Bank of Georgia	Georgia	51 mln USD	100
13	06.05.15	Bank Petrocommerce-Ukraine	Ukrainian investors	Ukraine	3.86 mln RUB.	96,5
14	15.06.15	Omega Bank	Ukrainian Business Group (UBG)	Ukraine	32 mln UAH	100
15	17.07.15	Astra Bank	AgroHoldings (Ukraine) Limited / NCH Capital	Ukraine/ USA	92,1 mln UAH	100
16	25.11.15	Raiffeisen Bank Aval	EBRD		-	30
17	12.01.16	UkrSotsbank	ABH Holdings S.A.	Luxemburg / Russia	9.9% stake in ABH Holdings (estimated at EUR 296.3 million)	99,9
18	04.08.16	ProminvestBank	OTP Group	Hungary	1.3 - 2 billion USD	100
19	30.10.16	Universal Bank	TAS Group	Ukraine	-	100
20	17.11.16	Інвестбанк	Uwe Christian Eshner	Austria	58 mln UAH	100
21	18.12.16	Private Bank	Ministry of Finance	Ukraine	1+ 148 billion UAH	100
22	08.02.17	Express Bank	Industrialbank	Ukraine	-	100
23	04.04.17	Sberbank Russia	Norvic Bank	Latvia, Russia	130 mln USD	100
24	09.06.17	Ukrainian Bank for Reconstruction and Development	Bohai Commodity Exchange Co., Ltd	PRC	82,827 mln UAH	100
25	18.09.17	VS Bank	Sberbank Russia	Russia	-	99,9

\* Note: compiled by the author by sources [26]

Delta Bank has grown fourfold due to the active buying of loan portfolios and banks over the past two years. 100% of the shares of the 55th largest financial institution of the country - Swedbank - were purchased [71].



It is possible to note that there is likelihood that only large ones with strong western market positions will remain on the market and will not show a desire to sell their assets at relatively low prices.

The growth in the number of merger and acquisition transactions is a hallmark of time and of the components of globalization of the world economy, but they also determine the nature of the domestic market and anticipate the adaptation of existing organizational and economic factors, taking into account the peculiarities of the functioning of international companies and banks in Ukraine. Therefore, only consolidation of experience, opportunities and rational management, marketing, financial and organizational decisions will allow to effectively use market potential of domestic enterprises and financial institutions.

### **2.3. Assessment of the «Credit Agricole Bank» value for mergers and acquisitions**

As already mentioned in the first section, all currently available methods for assessing the cost of business are divided into three groups: methods of income, comparative and asset approaches. At the heart of each approach lies a unique factor (or group of factors), which becomes the basis for building the entire methodological base of the company's costing formula.

Accordingly, the use of a particular assessment approach involves the use of a particular method of calculation and the use of certain types of information (for example, retrospective, current or forecast). Thus, the assessment of the value of a business income approach involves the use of income as the main driver of the company's value. When using a comparative approach, the company's price is calculated on the basis of information obtained on the market. Cost-based approach is based on costing, the introduction of which is necessary to create an analogue of the estimated company [74].

Despite the rather high degree of unification of most traditional valuation instruments, the application of parts of these tools relative to the assessment of financial institutions is very problematic and does not always yield credible results.

The general recommendations for assessing the value of banks, which are set out in the light of foreign practice, are not suitable for Ukraine due to:

- high and weakly predicted changes in the performance indicators of the banking sector in Ukraine;
- low informational transparency of domestic banks;
- insufficient level of stock market development and lack of relevant statistical information [41].

The valuation of a bank based on an income approach is carried out subject to the following conditions:

- An estimator should be able to identify future earnings with a sufficient degree of probability;
- The development of the bank should occur at a projected pace.

In order to assess the value of PJSC "Credit Agricole Bank" we will use an income approach. The income approach has the following valuation methods: discounted cash flow method, capitalization method, excess profit method, cost / income ratio method, attached profit method. The choice of a particular method of evaluation depends on information provided by the bank, a study of the bank's activities for a certain period, the features of the bank, the country in which it is located, and the prospects for development. The methods of excessive profits, the value-added ratio, and the profit and profit added are usually used by enterprises where the devices, technologies and means of production for products are used, they are more depreciated and change with technical progress. More universal methods and methods used are more often the method of capitalization of income and the method of discounting cash flows.

The method of capitalization of income should be used if a stable return is expected. If you look at the income schedule of the bank over the past 5 years we can see a stable growth trend (fig.2.2).

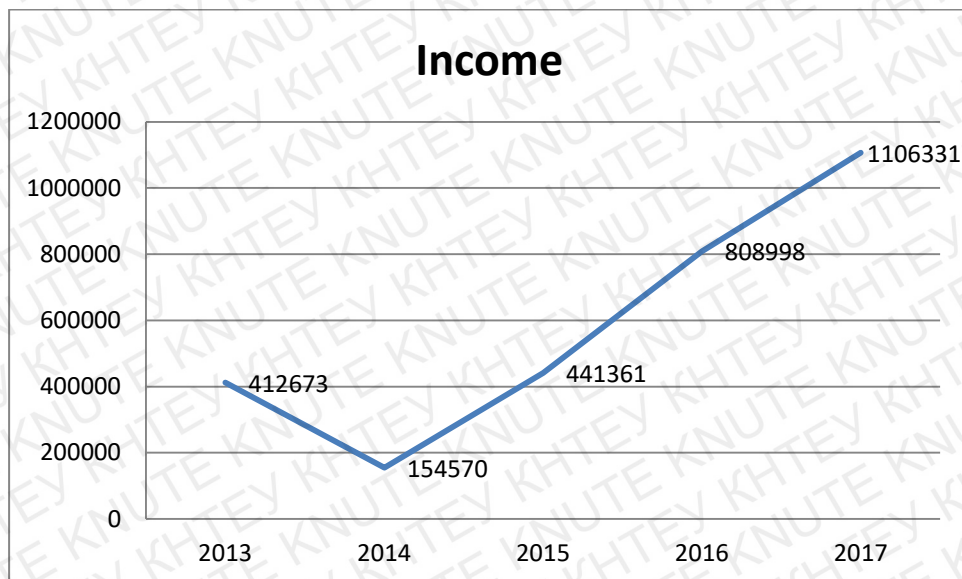


Fig. 2.2. Income of PJSC " Credit Agricole Bank " for the period of 2013-2017(ths. UAH)\*

\* Note: compiled by the author by sources[36]

Let's start with looking at the main financial indicators of the institution over the past 3 years (tab.2.3). The method of capitalization of net income measures the efficiency of the use of all assets in terms of their ability to generate income. The



evaluator gives a conclusion on the dynamics of income and chooses the rate of capitalization.

Table 2.3

**Key performance indicators of Credit Agricole Bank, ths. UAH\***

<b>Indicators</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Interest income	2 866 490	2 851 788	2 790 404
Interest expense	-837 128	-989 115	-914 889
Commission income	647 130	781 781	920 702
Commission costs	-133 944	-171 520	-202 069
Result from revaluation foreign currency	141 410	186 060	26 361
Deduction to reserve under impairment of loans and debts customers and other financial obligations	-1 177 687	-784 544	-275 371
Loss before tax	570 047	998 130	1 352 332
Profit tax benefit / expense (-)	-128 686	-190 344	-242 831
Profit for the year	441 361	807 786	1 109 501

\* Note: compiled by the author by sources[36]

The more substantiated values for the cash flow and the rate of capitalization, the greater the weight for the potential buyer will be the assessment received by this method.

To do this, we perform the following steps:

1. Election of the type of income of the banking institution that will be subject to capitalization.
2. Determination of the capitalization rate.
3. Determine the value of the institution.

So, our first step is to choose the kind of income and determine the number of data to be used in the analysis.

Taking into account the indicators presented in Table 2.4, the most suitable for applying for-for-payments in accordance with the chosen method of determining the value of a financial and credit institution as a form of cash income are interest

income, since they occupy the largest share in the activities of any financial institution, in The number we surveyed by the bank. Table 3.3 shows the dynamics of the level of interest income of Credit Agricole for 2017.

Table 2.4

**Dynamics of interest income of Credit Agricole for 2018 in terms of quarters, in ths. UAH\***

<b>Indicators</b>	I q. 2018	II q. 2018	III q. 2018	IV q. 2018 (forecast)
Interest income, thousand UAH	792 998	1 644 583	2 595 789	2 890 563
Growth rate, %		107,4	57,8	11,355854
Average growth rate,%				58,860876
The average percentage of income, thousand UAH				1980983,3

\* Note: compiled by the author by sources[36]

Having analyzed the interest income of Credit Agricole Bank and created a forecast for the 4th quarter of 2018, we have everything we need to determine the flow of selected cash flows for 2015-2018 (see Table 2.9)

Table 2.5

**Interest income of Credit Agricole Bank for 2015-2018\***

<b>Indicator</b>	2015	2016	2017	2018
Interest income, thousand UAH	2 866 490	2 851 788	2 790 404	3 622 310
Growth rate, %		-0,51289	-2,15247	29,813102
Average growth rate,%				9,0492454
The average percentage of income, thousand UAH				3032748

\* Note: compiled by the author by sources[36]

The second step is to determine the rate of capitalization. To determine the capitalization rate, we propose to use the following formula:

$$R = \frac{r-g}{100+g} \quad (2.1)$$

where: R - capitalization rate;

r - discount rate;

g - projected average growth, based on the analysis of retrospective data of the relevant company (institution) [51].

In our view, and given the available information base necessary for determining the rate, it is advisable to calculate the discount rate on the basis of the CAPM model. The main components of the model are:

- Risk-free rate;
- Beta-factor;
- Market risk premium;
- Other additional risk supplements, for example, with a small bank size, specific risk of the bank being valued, etc. [41].

The formula for calculating this model is as follows

$$k_e = R_f + \beta (R_m - R_f) + S_1 + S_2 \quad (2.2)$$

where:  $k_e$  - the required rate of profit;

$R_f$  - Risk free rate;

B - beta coefficient;

$R_m$  - is the average market rate of return, determined on the basis of long-term general profitability of the market;

$(R_m - R_f)$  - market risk premium;

$S_1$  - the risk associated with the small size of the bank;

$S_2$  is a specific bank risk [41].

In international practice, the risk-free rate of return is the yield rate on long-term government debt obligations. In domestic banks, it is appropriate to accept the official rate of refinancing as a risk-free rate. From 25.10.2017, the NBU has set the refinancing rate at 18% per annum [49].

The calculation of this model takes into account the premium for the country's risk, which reflects the additional income that the investor will require for the risk



associated with investments in the Ukrainian economy compared with the economy of the most developed countries, such as the United States.

A. Damodaran proposes to use the following calculation approach for taking into account the risk premium country [75]:

$$(R_m - R_f)_I = (R_m - R_f)_E + CRS \quad (2.3)$$

where:  $(R_m - R_f)_I$  - market risk premium on the market of the bank country;

$(R_m - R_f)_E$  - market risk premium in the reference market (US market);

CRS is a spread, which is determined by the sovereign credit rating of the country.

On the official website of A. Damodaran, annually there is data on the level of risk premium in most countries of the world. As of 01.01.2018, the premium for Ukraine's risk amounted to 10.38% per annum [82].

In addition, the official website of A. Damodaran provided information on the value of the beta factor of the industry. If we talk about the banking sector, then according to this resource, it is 2.85% for the current period under study [82].

Thus, by substituting the corresponding data for our formula, we obtain:

$$k_e = R_f + \beta (R_m - R_f) = 0,18 + 0,285 * 0,1038 = 20,95\%$$

The forecasted average growth rate of PJSC "Credit Agricole Bank" is shown in Table 2.9. Thus, we have all the necessary data to determine the capitalization rate:

$$R = \frac{20,95 - 9,05}{100 + 9,05} = 0,109\%$$

The last third step is to multiply the capitalization rate by the chosen type of income:

$$V = \frac{I}{R} = \frac{3032748}{0,109\%} = 27\,791\,695 \text{ (ths. UAH)}$$

Where: V – value;

I – income;

R- capitalization rate

For a more objective assessment, we propose to apply one more way to estimate the value of a company based on the cost approach, since it is not less

widespread than revenue-generating. From the methods of the cost approach, the method of net assets was chosen to calculate the value of Credit Agricole Bank. This method reflects the activity of the bank, shows each article of the balance sheet. To do this, we calculate the value of each asset in the balance sheet, and then determine the current value of the obligation.

The calculation is based on the data of the Consolidated Statement of financial position as at 31 December 2017 PJSC "Credit Agricole Bank" is taken from the official website of the bank (appendices B, C).

*Table 2.6*

**Calculation of net assets of Predatory Credit Agricole Bank as of  
December 31, 2017, ths. UAH.\***

	31 December 2017
<b>ASSETS</b>	
Cash and cash equivalents	8 708 812
Due from other banks and NBU	1 108 974
Loans and advances to customers	19 393 162
Securities in the Bank's portfolio available for sale	1 065 426
Investment property	5 797
Deferred tax asset	12 396
Property, equipment and intangible assets	560 222
Other financial and non-financial assets	88 644
Non-current assets held for sale	1 597
<b>Total assets</b>	<b>30 945 030</b>
<b>LIABILITIES</b>	
Due to other banks	14 448
Customer accounts	26 064 290
Other borrowed funds	2 770
Current income tax liabilities	47 552
Provisions for liabilities	106 592
Other financial and non-financial liabilities	368 624
Subordinated debt	1 076 750
<b>Total liabilities</b>	<b>27 681 026</b>
Net Assets	3 264 004

\* Note: compiled by the author by sources[42]

After the calculations (Table 2.6), we see that the value of predatory Credit Agricole Bank by the asset approach of net assets by the end of 2017 is 3 264 004 thousand UAH. We will also consider the cost of Credit Agricole Bank which will be calculated at this point according to the nine months of 2018 (Table 2.7)( appendices D, E).

*Table 2.7*

**Calculation of net assets of Credit Agricole Bank as of September 30,  
2018, ths. UAH.\***

	30 September 2018
<b>ASSETS</b>	
Cash and cash equivalents	9 013 357
Due from other banks and NBU	1 504 142
Loans and advances to customers	23 174 525
Securities in the Bank's portfolio available for sale	996 241
derivative financial assets	7 013
Investment Property	5 357
deferred tax asset	13 523
fixed assets and non-tangible assets	560 350
other assets	150 306
Property, equipment and intangible assets	9 438
<b>Total assets</b>	<b>35 434 252</b>
<b>LIABILITIES</b>	
Due to other banks	9 186
Customer accounts	29 903 351
Derivative financial liabilities	17 539
Other attracted funds	1 991
Commitment to current income tax	87 703
Provisions for obligations	85 009



Other obligations	315 470
Subordinated debt	1 087 179
<b>Total liabilities</b>	<b>31 507 428</b>
Net Assets	3 926 824

\* Note: compiled by the author by sources[42]

According to the calculations, the value of the bank in 2017 is UAH 3 264 004 thousand UAH. Thus, we see that by the net asset value method, the bank's value for the 9 months of 2018 increased by 662 820 thousand UAH. and reached 3 926 824 thousand UAH.

Usually, the calculation of the cost of the bank according to the cost approach of the net asset method should be, but there are many reasons why the given method is not used in practice. For such reasons include:

1. Only the balance sheet data is taken into account at the time of the formation of the balance sheet items. That is, the data contained in the bank statements for the year are taken into account in the report on the financial condition of the bank for a specific date of its formation.

2. Macroeconomic indicators are not taken into account: demand, level of solvency of demand, inflation, etc.). Particular attention should be paid to inflation, which has an impact on any value, and on each balance sheet.

3. Depends on the accepted accounting policies. Each bank defines itself on the basis of the "Regulation on the organization of accounting, accounting control in the conduct of operations in the banks of Ukraine", according to which develops the system and forms of management accounting, internal accounting and control of operations, defines the rights of employees to sign documents, approves rules document flow and processing technology for accounting information, an additional system of accounts and registers of analytical accounting. Therefore, when assessing the bank's value, we see such a balance of the bank as it wants to show us the bank.

4. The price should be based on the price increase at the time of the evaluation. That is, since the calculation may be later than the publication of the report, the actual price of the articles, taking into account all factors could change.

5. The activities of the bank are not taken into account directly. That is, there is no data on the bank's income, it has a gain or loss for the reporting period, etc.

because of these reasons, even such a simple calculation of the bank's cost has many disadvantages. And how do we see the difference in value in 9 months: 2017 - 3 264 004 thousand UAH, 30.09.2018 - 3 926 824 thousand. UAH

In general, Ukrainian scholars do not use methods of cost approach to estimate value, since its application is complicated by the implementation of elementary estimation of the value of assets and liabilities of the bank, not taking into account a number of important factors and the lack of information for calculation or unreliability of these banks.

Consequently, we calculated the cost of the bank by the expense approach, namely, the net asset method for the two periods, and received a value of UAH 3 264 004 thousand as at 30.09.2018. and 3,924,824 as of December 31, 2017.

More truthful, in our opinion, is the valuation of the value of Predatory Credit Agricole Bank by the income approach, namely the capitalization of income. The cost of the bank is 27 791 695 thousand UAH.

### **PART III.**

## **WAYS TO IMPROVE THE MERGER AND ACQUISITION PROCESS OF BANKS.**

### **3.1 Foreign experience of mergers and acquisitions of banks.**

Mergers and acquisitions have a fairly long history, but especially over the last two decades, they have become a key factor in economic development. They not only have a huge impact on all sectors of the world economy, but also facilitate the improvement of organizational structures and diversification of companies. Moreover, mergers and acquisitions lead to the emergence and development of new technologies and market segments, as well as to reduce aggregate and unit costs and to minimize risks.

Based on commonly accepted foreign approaches, mergers and acquisitions are part of a corporate strategy and an important component of the company's management system associated with the process of buying, selling, dividing or merging various enterprises, helping companies to operate effectively and quickly evolve.

Recently, multinational banks, both in economically developed and in developing countries, have been involved in the restructuring and merger process, which greatly changed the nature of business in the banking sector. Changes in the legislative regulation of banking business and technological innovations have substantially increased competition in the banking sector, including the opening of new markets for expansion.

In many countries, the bankruptcy of the largest banks as a result of banking crises gave an additional incentive to restructure and process local and transnational mergers and acquisitions in the banking sector. The advances in the development of IT technologies, the ongoing globalization of capital markets and the process of risk management, also led to the merger in investment and insurance banking business.



Mergers are not always caused by problems. Moreover, activity in M & A - both in terms of the number of these deals and their size - peaked on the eve of the global financial crisis of 2008, including international treaties within the Eurozone and beyond. After the peak of 2007, this activity went down, more important was the internal restructuring, especially in Greece and Spain, which had to implement a difficult correction program.

It should be noted that the method of mergers and acquisitions does not always help. In October 2007, a consortium created by Royal Bank of Scotland (RBS), Fortis and Banco Santander, acquired the ABN AMRO bank. This agreement is still the largest banking takeover in history. But soon RBS and Fortis had to be rescued, who were on the brink of bankruptcy [4].

In terms of banks, international mergers can potentially be more attractive if they occur within a territory with general supranational supervision. In this case, you can take advantage of the existence of the single supervisory and sanitation authorities.

Recent changes in the regulation of the banking sector in the Eurozone, now under the supervision of the ECB and received by the Bank's sole reorganization body, reflect an understanding of the benefits of cross-border mergers. However, while Europe lags behind in such mergers, due to the lack of financial integration in the broader sense.

In the European Union, national banks tend to be dominant players in domestic markets, such as BNP Paribas in France, UniCredit in Italy. In the USA, by contrast, large banks, such as Bank of America, JPMorgan Chase, Wells Fargo, are dominant in many states.

American banks have more space to diversify. And European banks, in the process of international mergers, are forced to operate in the conditions of enormous differences in culture, language and legislation. And this is extremely difficult, especially considering that many of these banks still need to radically reduce excess capacity. As a result, in the short term, European banks will most likely be engaged in internal consolidation or, at most, regional.

In the UK, which voted in June 2016 on leaving the EU, the situation is particularly complex. The country has long enjoyed the benefits of an open foreign-sourcing policy, which allowed, for example, the Spanish Group of Companies to begin absorbing the British bank Ajac Keiopai in 2001 [3]

In analyzing the processes of concentration of banks in the countries of the European Union should also take into account such difficulties. First, cross-border mergers are difficult to implement because, because of the strategic nature of the banking sector, state-owned local authorities seek to maintain supervision over them, despite the tendency towards deregulation, as well as preventing the purchase of local banks by foreign ones.

Secondly, as noted above, most EU countries have a widespread network of local banks, so it is difficult to get into this network by a foreign bank; in addition, the creation of a network requires significant investment without any guarantee of their quick payback. Acquisition of an existing branch network in many cases is virtually impossible, in particular, because of the high selling price, which can reach the amount, 20-30 times higher than the annual profit of the acquired bank.

Thirdly, the persistence of cultural differences between EU countries results in different behavior of consumers of banking products and services, as well as varying degrees of trust in their "own" and "foreign" banks.

The leading banks of the EU countries carry out an active European strategy, striving not only for mergers and acquisitions, but also to search for individual niches in the partner countries (for example, in the field of financial engineering, leasing, etc.), which allow to expand the scope of activities and increase profitability. To this end, partnership agreements and cooperation with local banks and other financial institutions are signed. The number of such transactions in recent years significantly exceeds the number of mutual participation, mergers and acquisitions. The most widespread form of cooperation between the largest European banks is the so-called strategic alliances.

The forms of inter-bank co-operation in the EU are very diverse:

1. The most simple form is technical cooperation, for example, in the implementation of joint research programs or the exchange of trainees.
2. A more complicated form of commercial co-operation is when banks provide some services (for example, loans) to clients of partner banks.
3. Creation of joint branches, which, as a rule, specialize in carrying out certain operations.
4. Joint development and use of new banking products, such as venture capital and mutual funds funds.
5. Mutual shareholding and placement in the boards of the banks. With the help of such participation, the largest banks of the EU countries seek to ensure their presence in the markets of partner countries.

In order to increase the competitiveness of the Ukrainian banking sector, it is important to ensure the following measures, taking into account the specifics of the European market model for mergers and acquisitions in the banking sector:

1. Strengthening the role of the state in the processes of mergers and acquisitions in the Ukrainian banking sector. Positive European experience shows the effectiveness of the role of the state in the processes of mergers and acquisitions, which most manifested itself in the post-crisis period. This was reflected in the provision of emergency loans to banking institutions, as well as the direct entry of governments into the capital of the most troubled banks.
2. Activation of use in merger and acquisition transactions of joint ventures and other associations of banking groups. As the experience of France shows, in the way of the creation of joint ventures, banks, on the one hand, retain control over key services, and on the other, they use the scale effect in those areas that have suffered the devastating effects of the financial crisis to save financial resources.
3. Stimulation of mergers and acquisitions. During the financial crisis, the European bank recorded an increase in the number of acquisitions by traditional banking groups in private banking and asset management.



4. Sale of non-core banking subsidiaries, usually institutions experiencing difficulties during the crisis.

5. Intensification of the merger between savings banks. In this aspect, for the Ukrainian banking sector, this experience is a positive example of the successful merger of even direct competitors, which not only does not reduce overall competition, but also solves a number of important tasks: from increasing the competitiveness of the newly created institution to improving the state of the banking sector as a whole.

6. Intensification of sales of loan portfolios as an important means of increasing liquidity and reducing the level of indebtedness. The European experience of selling non-core assets or low-quality loans has shown the high ability of these instruments to enhance the competitiveness of banks.

7. Stimulation of cross-border mergers in the banking sector of Ukraine. Ukraine, which is actively developing international integration, can look at examples of successful consolidation in the European banking sector, driven by technological advances, deregulation and increased competition. Consolidating the competitive advantages of Ukrainian banks beyond national borders is a challenge at the same time, but it also contains powerful prospects for strengthening the competitiveness of domestic banks. At the same time, EU practice proves that successful competition in the international market should precede the consolidation of the banking sector within national territories and the creation of national leaders beforehand [47].

In the context of the current trends in the world financial market, the study of the improvement of international banking mergers and acquisitions shows their close connection with the process of transnationalization of these financial structures. Currently, it is established that one of the main reasons for their advancement to markets in other countries is the search for new customers. At the same time, this kind of aspiration is often combined with banks with the ability to increase profits and expand their position in the national market.

According to Bloomberg Global Legal Advisory Mergers & Acquisitions Rankings, in 2015, the record number and value of M & A transactions amounted to

4.3 trillion. dollars The United States, and the number is 48,124 deals. The previous record year for mergers and acquisitions was 2007, where the total amount of transactions for the year amounted to 4.14 trillion. dollars The United States, and the number of 47,761 transactions [87].

The global M & A market demonstrated its sustainability in 2016, reaching \$ 3.9 trillion, thus providing the third record year (see Figure 3.1). In addition, 2016 provided the largest volume of deals made since 2008 and a decrease of 18% compared to the previous year the value of M & A transactions. Lastly, a 39% reduction in the value of "megauploads" (worth starting at \$ 10 billion) was affected, while deals worth up to \$ 250 million fell slightly lower, 6% a year [86].

Summarizing the analysis of the banking markets of M & A in Europe, one can distinguish the most significant trends that have a significant impact on the increase of M & A activity in the given field:

- globalization of financial markets;
- economic crises;
- deregulation policy, which means weakening the regulation of banking activity by the state;
- increasing global competition, especially by American megabels, which pursue a dominant strategy on the global market and seek to take advantage of the single economic and financial space within the EU;
- a decrease in the margin of bank profits and competition from non-banking institutions, especially insurance companies that have recently been actively buying up investment banks;
- getting rid of unnecessary banking "capacities" and streamlining activities, as today Europe is "crowded" with banking branches;
- the desire to achieve economies of scale. The use of state-of-the-art information technology encourages banks to expand their business to reimburse incurred expenses. Earning savings not only on a scale but also by expanding the range (range) of products and services offered, as well as the recent tendency to

reduce the interest margin on profit, forces banks to buy insurance companies or other financial institutions or develop their cooperation with them. An important trend in the development of banks is also the strengthening of universalization and diversification, which is stimulated by US and EU legislation, and leads to the erosion of differences between different types of lending and financial institutions. Diversification of banking allows: to use the existing network of departments more efficiently; allocate costs to a wider range of activities; reduce fluctuations in income; reduce interest, market and other types of risks; to receive significant savings from expanding the range of banking products and services;

- the need to diversify risks by acquiring shares in the capital of other banks. To solve this problem, banks expand the network of foreign branches and offices, as well as take part in the capital of foreign banks;
- demands from shareholders to increase the return on equity of banks. It forces to expand and rationalize activity, including at the expense of consolidation of banks.

For the banking sectors of the EU countries are characterized by their specific features. The cross-border agreements are rather problematic because of the above reasons, but nevertheless the leading banks of the EU countries carry out an active European strategy, striving not only for mergers and acquisitions, but also to search for individual niches in partner countries. The most common form of cooperation between the largest European banks is the conclusion of so-called strategic alliances.

Ukraine has made a very modest contribution to the global index. The volume of all mergers and acquisitions in the Ukrainian market was within \$ 1 billion. The USA, and the agreements themselves belonged to the category of technical [1]. The domestic banking system lags far behind the European countries by the level of capitalization of banks. One of the options for a possible increase in capital is mergers and acquisitions. This is also one of the requirements of the IMF, reducing the number of banks through the implementation of the merger and acquisition. However, by this time, the NBU has not registered a bill to submit to the Verkhovna Rada of Ukraine on simplification of the merger and acquisition procedures of banks.



Thus, the Independent Association of Ukrainian Banks proposed to reduce this procedure by submitting a package of documents simultaneously to the NBU and the Antimonopoly Committee of Ukraine. However, this news appeared in the media as of 22.02.2016, and by this time the proposal is only a proposal. Another condition that impedes the active process of mergers and acquisitions in the banking system is the significant risk of merging with troubled banks or banks that could lose their license in the notorious past [2].

International practice suggests that M&A processes are actively used to increase the capitalization of the banking system. The largest mergers and acquisitions of banks in the amount of authorized capital are four US banks: JP Morgan, Bank of America, Citigroup, Wells Fargo, which use this mechanism.

In Ukraine, there are few cases where banks use mergers and acquisitions. First of all, banks with 100 percent foreign capital were initiators: Raiffeisen International, VolksBank International AG, SvedBank, Erste Bank. Domestic banks have access to a larger material base, international management experience, and the use of a model of optimized flexible processes. Foreign banks, in their turn, seek to expand the geographical boundaries of their own influence and be able to function in the banking market at higher rates than their domestic ones [1]. Given the political and economic crisis in Ukraine, the interest of foreign investors in the domestic banking system has decreased, which is why the increase in the number of merger and acquisition processes with foreign banks in the near future should not be expected.

In the near future, the factors influencing the development of the domestic market of mergers and acquisitions will be: stabilization of the general economic and political situation, forecasting of the dynamics of the exchange rate, harmonization of the expectations of participants in the processes of mergers and acquisitions regarding the value of assets of Ukrainian banks, restoration of the stability of functioning of world credit markets. Synergy of financial institutions is urgently needed in Ukraine for the general strengthening of the country's system. The combined efforts will help to easily survive the situation in Ukraine, but also to reach a new stage of development.

Thus, by studying the experience of leading foreign countries, it is clear that the implementation of the stimulation of mergers and acquisitions in the banking sector has many positive effects, namely:

- crowding out of the market for inefficient banks through mergers and acquisitions;
- a sufficient number of positive effects of mergers and acquisitions at all stages of the economic cycle, both during the downturn and growth stages;
- maintaining healthy competition in the market and maintaining the competitiveness of the banking sector through adherence to a consistent antitrust policy in regulating the merger and acquisition process of banks;
- expansion of the client base of newly established banking institutions through the application of reorganization procedures;
- optimization of financial resources in the implementation of mergers and acquisitions, which may be an advantage over the liquidation of the bank;
- expansion of competitive positions of banks in the market at the expense of mergers and acquisitions, in the medium-term perspective. The sharpening of competition in the banking sector is due to the dynamic expansion of the range of financial services, as well as the deepening of the liberalization and openness of national banking sectors. This leads to a tendency for even competitive banks to engage in mergers and acquisitions in order to consolidate their competitive positions [47].

The development of financial and economic relations between different countries has led to the expansion of the geographical boundaries of the activities of strong players in the market, which has manifested itself in the processes of globalization and liberalization. These processes could not have escaped the banking sector; therefore, at this stage of development, financial and credit institutions most often choose an instrument to increase their competitive positions and opportunities to maximize profits, namely, M & A transactions.

As the banking sector in Ukraine is only in the process of becoming, we have analyzed the world experience that could become a model for improving M & A

processes in the domestic money market. The leaders in the number of mergers and acquisitions are the United States, the leading Pacific countries and developed countries of the European Union. The peculiarities of mergers and acquisitions in these countries are, firstly, the introduction of specialized legislative acts on the part of regulators, which were called to regulate and supervise the lawfulness of such agreements, and secondly, the avoidance of monopolization by one institution of the entire market in order to maintain a competitive relationship among the participants in the banking sector.



### **3.2. Identification of the main problems and ways to improve the mechanism of realization of the process of mergers and acquisitions of banks in Ukraine.**

The total number of banks in Ukraine is decreasing, but despite this, the total assets of all banks in 2016 increased by 3.6% and amounted to 1 trillion 299 billion hryvnia by comparison with the previous year, where as of 01.01.2015 assets amounted to 1 trillion of 254 billion hryvnias, and as of 10.1.2017, the assets of banks decreased and amounted to about 1 trillion 212 billion hryvnia. This, in turn, caused a deterioration of the monetary situation in the country, and currency fluctuations in the country [88].

Ukraine's banking system for the third consecutive year is unprofitable in 2016, the banking system in Ukraine suffered losses of UAH 158.967 billion, up 138.7% year-on-year (UAH 66.6 billion in 2015). As practice shows, no bank is insured against bankruptcy, regardless of the size of its capital, organizational structure or membership of a particular sphere of the economy [48].

The reasons for such effects can be divided into three groups:

- aggravation of the financial crisis in the world and in Ukraine;
- absence of the developed strategy and tactics of work in market conditions;
- imperfection of NBU monetary policy regarding commercial banks;
- insufficient capitalization of the banking system [69].

The capitalization of the banking system, as one of the most important characteristics of its development, reflects the sufficiency of capital in the economy, as well as the prospects for further development of the national economy [69].

The main consequence of increasing the capitalization of the banking system is to increase the activity of consolidation of individual institutions. The strategic goal of the consolidation of commercial banks is to increase the reliability and stability of the banking system of Ukraine and a separate commercial bank, ensure the capitalization of the banking system and stable operation of the payment system, protect the interests of creditors and depositors, improve the financial condition of commercial banks, increase the efficiency of activities due to the concentration or

division of capital of banks, expansion or specialization, reorientation of banks activity and increased confidence in these banks (or newly created banks) nku)

The features of consolidation of banks in the Ukrainian market are the absorption by a foreign investor of the Ukrainian bank for the purpose of its further resale. The large number of investors who only announced their arrival in Ukraine were on the list of assets for sale, buying up banking assets only to expand the international structure of their business, and therefore did not actively develop their business in Ukraine.

Today, the crisis period in the consolidation market of Ukrainian banks has the following characteristics:

- 1) a sharp fall in the value of banks to be acquired;
- 2) change of main groups of buyers;
- 3) other motives for the purchase of banking institutions, due to the difficult situation in domestic and world banking markets;
- 4) mass withdrawal of their deposits by depositors of banks, which forced banks to revise their strategic policy, to stop development programs and reduce costs by optimizing activities [87].

Thus, if before the crisis, the bank's cost was predominantly determined by the opportunities that a buyer would receive in view of the future expansion of banking activities due to the developed technological platform and developed regional network, then in the crisis period, the main indicators are the reputation of the bank, the status quo with the quality of credit portfolio, client base stability and risk management mechanism [86].

Analysed the problems faced by Ukrainian banks during M & A processes, we can identify the main reasons that lead to negative consequences in the process of reorganization:

- 1) imperfect policy regarding the mergers and acquisitions of banks by supervisors and regulators. Much of the abuse and mishandling in M & A is due to imperfect legislation that impedes the conclusion of fair treaties and contracts. The

processes of reorganization require significant supervision and targeted regulation by the National Bank of Ukraine.

Procedures, which are prescribed in normative and legislative documents of Ukraine, require detailed definition and description. The terminology that formulates the value of mergers and acquisitions must be clearly articulated. On the part of the antimonopoly authorities of the state too much attention is required to the realization of merger (absorption) processes;

2) lack of experience in employees who are engaged in mergers or acquisitions. The large number of errors in this industry arises as a result of insufficient experience of managers and business owners. M & A planning requires foreign experience to be taken into account, while taking into account legal and technological issues, analyzing the effectiveness of a bank's acquisition decision and assessing its value, analyzing whether the draft decision on the acquisition is consistent with the bank's strategy and how effective the management of the bank is after reorganization. Strategic M & A decisions taken by Ukrainian banks are characterized by complex and time-varying funding structures, complex tax burden schemes, non-transparency and unpredictability of the corporate governance system;

3) a reassessment of synergistic and other positive effects derived from mergers or acquisitions is required. Each bank that buys a new business through mergers or acquisitions aims to create a strategic advantage by joining and integrating new business segments that need to become more effective than the internal development of this bank. In the banking sector, the main advantage of mergers and acquisitions prior to increasing the bank through domestic sources is the possibility of obtaining a synergistic effect, reducing costs and using a variety of bank products and services, conditioned by the rapid achievement of the goals set by the credit institution and, due to increased activity, leads to weakening competitive pressure, and also helps to increase the geographical presence of the bank and expands the client base.



The reorganization and restructuring of banks envisages financial rehabilitation and ensuring the stable functioning of the banking system as a whole, increasing the concentration of bank capital through mergers, mergers and mergers of banks, as well as improving the relevant aspects of banking regulation and supervision. An important condition for the effectiveness of further development - increasing the level of capitalization, competitiveness and liquidity of domestic banks.

In order to limit the negative effects of mergers and acquisitions and prevent price increases, excessive concentration of capital and anticompetitive behavior, the state needs significant control. In developed countries, the main areas of such control are:

- antitrust regulation, since the direct value of M & A transactions depends on the amount of tax payments, the state must regulate the taxation system;
- regulation of transactions related to securities.

In the context of these facts, are appropriate to following main ways of improving and improving the efficiency of mergers and acquisitions in the banking sector of Ukraine.

1. The current legislation and regulatory framework of the National Bank of Ukraine regarding mergers and acquisitions needs to be improved as well as to weaken administrative barriers in the agreements of the banks' association until Ukraine achieves the desired level of concentration of bank capital and formulate certain market mechanisms that would contribute the development of reorganization processes. Therefore, in our opinion, it is important to introduce a special law that would control and introduce transparency in the relevant processes.

The development of conditions for ensuring the competitiveness of banks in the process of mergers and acquisitions should be aimed at ensuring the complexity of reforms. This involves regulating the following areas of activity that will be prescribed by the relevant regulations at the state level:

- simplifying the process of obtaining permits and registering a newly created institution;

- shortening the duration of the merger and acquisition procedure; improvement of all phases of the merger and acquisition process;
- creation of a centralized system of public analysis of mergers and acquisitions of banking institutions on a permanent basis at the NBU;
- harmonization of normative legal acts acting in the field of mergers and acquisitions, based on international experience;
- raising the responsibility of banking institutions for violating antitrust laws that caused losses to depositors, shareholders and customers;
- Institutional strengthening of the protection of depositors' rights, the development of transparent mechanisms for public control of mergers and acquisitions in the banking sector;
- raising the awareness of shareholders, depositors and clients of banks about mergers and acquisitions;
- reventing the creation of super-large banking institutions, with high risk-taking systems for the banking sector;
- implementation of new principles of antitrust laws and coordination with NBU's licensing mechanisms;
- reorientation of state control and supervision to detect and punish abusive absorption for its prevention and prevention;
- improvement of regulatory development on the basis of analysis of regulatory influence and public discussion of draft normative legal acts in the field of mergers and acquisitions of banking institutions;
- streamlining reporting and other information requirements for M & A banking institutions.

2. To obtain a positive result, it is necessary to introduce modern methods in the banking sector of Ukraine that will help to stimulate bank mergers and acquisitions. It should be noted that the domestic state practice on stimulating mergers of banks is very differentiated, and the methods used in this case have both administrative and market character (granting of privileges, liberalization of

legislation, reduction of the role of the state in the banking system, administrative regulation, etc.).

3. Mergers and acquisitions of banks need to increase the efficiency of these processes. One of the important directions that solves the problems of bank reorganization is the correct justification of the effectiveness of mergers (takeovers). Improving the efficiency of reorganization processes depends on the growth of capitalization, regulation and diversification of risks, cost reduction, etc.

4. The bank's ability to accumulate cheap credit resources through the implementation of arbitration operations is significantly limited by the lack of a developed financial market. Therefore, stimulation of the development of the market for corporate control and the domestic stock market is an important direction in improving the efficiency of mergers and acquisitions.

The key areas of M & A regulation in the context of increasing the competitiveness of Ukrainian banks are to ensure optimization of banks' activities by taking them from consolidation effects. In this context, increasing the competitiveness of banks due to the impact of mergers and acquisitions and the formation of an appropriate structure (a combination of large banks with an extensive network of branches, regional, cooperative and specialized banks) is an important and urgent task [47].

For Ukraine it is expedient to implement the progressive experience of the EU, which is based on the existence of various forms of competition policy. They are aimed at solving M & A issues.

In our view, among the priorities that need to be addressed today in the area of banking supervision related to factors that will affect the market for mergers and acquisitions:

- raising the level of capitalization of banking institutions that are in the process of reorganization;
- improvement of methodical approaches to the regulation of transactions of banks that are in the process of reorganization with related parties;



- strengthening responsibility, including by establishing its criminal component, bank managers, significant holders and other related parties for activities that lead to the insolvency of newly formed banks or banks that are reorganizing;
- assessment of the quality of assets of banks that are in the process of reorganization in order to determine the need for additional capitalization of banking institutions and to ensure maximum transparency and promptness in providing this information to the competent authorities;
- further purification of the banking system from financial institutions that are insolvent, carry out money laundering and do not comply with the requirements of the legislation. At the same time, the relevant process should be deprived of manipulations based on insider information and corruption component in order to increase transparency, to publicly disclose the criteria by which banks are considered unreliable.

## CONCLUSIONS AND RECCOMENDATIONS

In the final qualification work, an empirical analysis of the essence of such concepts as mergers and acquisitions was conducted, the classification signs of consolidation processes were generalized, the world and national experience of mergers and acquisitions were analyzed, and a number of priority directions for improvement of these processes in Ukraine were proposed, taking into account world experience. According to the results of relevant research, a number of theoretical, methodological and practical conclusions and proposals have been formed:

1. During the study of theoretical aspects of the concepts of mergers and acquisitions, we considered them from two mutually complementary parties: economic and legal. Summarizing the opinion of domestic and foreign scholars and taking into account the interpretation of these concepts by the main legislative acts of Ukraine, we have proposed the definition of the concept of merging banks as the organizational and legal form of the emergence of a new institution through the voluntary association of two or more independent banks, with the subsequent transfer of all of its property rights, assets and liabilities. At that time, the absorption is defined as the organizational and legal form of the transfer of one or more financial and credit institutions of all its property, rights and obligations to another financial and credit institution - the successor, without preserving the last right to independent functioning.

2. The essence of the concepts of mergers and acquisitions has created the need for a generalization of the classification features of processes of concentration of capital in the banking sector, which distinguishes them in accordance with the goals, objectives and objectives of the parties concerned in these legal relationships to initiate these transactions.

3. The implementation of the merger and acquisition process is quite complex and lengthy. This is primarily due to the difficulties encountered in advancing each stage of the merger and acquisition (M & A). In view of this, we analyzed the features of each stage, both from the buyer's side and from the seller.

4. During the analysis of the steps of the M & A agreement, we found a strong link between the nature of the transactions, the circle of interested investors, and the financial status of the company's objectives. Equally important in the process of consolidation and the search for potential investors is the absolute confidentiality between the parties to the transactions, the real status of the company, its objectives, its business models and the essence of its competitive advantages, which provided it a suitable place on the market, considering this an important step is the stage signing a confidentiality agreement. In the most general form, the M & A transaction process will consist of the following stages: preliminary contact of all interested parties; preliminary due diligence (pre-investment research of the object of the agreement, which allows obtaining reliable and objective information about the institution in which the investment will occur, most often performed by a third party that is not interested in a particular outcome of the transaction); signing a memorandum of intent / agreement on mergers / acquisitions; ultimate due diligence; termination of the transaction, including determination of the target price of the target bank; closing the deal.

5. Any agreement is based on the definition of a mutually beneficial price for all interested parties. In this regard, we have generalized the main methodological approaches to assessing the value of a financial and credit institution. Traditionally, it is common ground to distinguish between three approaches to value estimation, namely: income, asset-based and comparative.

6. The main prerequisites for activation of consolidation processes in the banking sector were: adoption of the NBU Resolution "On bringing the authorized capital of banks to the minimum size" in 2014, which caused a sharp decrease in the number of banking institutions from 180 to 80, as of 10.1.2018 ; the financial crisis in Ukraine, which greatly worsened the loan portfolio of banks, increasing the proportion of loans that turned to the status of hopeless, and needed a large volume of reserve from banks, the crisis in the currency market.

7. For the purpose of practical application of the methods for assessing the value of a financial and credit institution, PJSC Credit Agricole Bank was elected by



us. In the selection of methods for assessing the value of the relevant commercial bank, and taking into account the peculiarities of its operation and development, we have selected two methods: the method of capitalization of cash income and the method of net assets. According to the results of the study, we came to the conclusion that the results of the implementation of the capitalization method are more objective.

8. The world-wide experience of M & A regulation demonstrates the need for specialized legislative acts that regulate the main areas of control and monitoring to ensure competitive conditions for functioning in the market of borrowed funds. It is noteworthy that the experience of such countries as: USA, Japan, Poland and Hungary (given the similarity of functioning and development of economies of these two countries to Ukraine). A common feature of American practice is to limit the possibility of territorial expansion of the banking business, in accordance with the model of the US territorial structure, each state has the right to implement its own legislative acts, which may differ substantially from one another. In addition, due to the degree of development of the financial market as a whole, the US faced the threat of monopolization of the banking sector by the largest players in the market, which prompted the government to introduce specialized legislative amendments.

The reorganization model in Japan is based primarily on respect for the principle of voluntariness and solidarity of the stockholders. Thus, the possibility of absorption is incredibly complicated, in other words, it is almost impossible. Thus, the structural feature of the Japanese economy is the cross-ownership, which results in closed negotiations among the owners of banking institutions.

In order to confirm the hypothesis of the impact of macroeconomic indicators on volumes of mergers and acquisitions, we conducted a correlation analysis whose main purpose was to prove the density of the link between the volume of mergers and acquisitions and macroeconomic indicators such as: GDP and NBU discount rate. The results of our research have shown that there is a very strong direct link between GDP and M & A volumes and a strong backward link between the discount rate and the volume of M & A transactions.

The main suggestions for improving the direction of regulation and efficiency of M & A transactions are as follows:

1. The main directions of improving the methodology of mergers and acquisitions are:

1.1. bringing the national banking system in line with the banking systems of the developed countries;

1.2. improvement of the regulatory base of the NBU on merger and acquisition processes;

1.3. stimulating the development of the domestic stock market in order to accumulate banks of alternative sources to raise funds;

1.4. implementation of foreign experience in the process of developing the methodology of mergers and acquisitions.

2. In order to improve the methodology of mergers and acquisitions and increase the level of successful transactions, it is important to create a centralized system of public analysis of mergers and acquisitions of banking institutions on the basis of data coming to the NBU; bringing the legislative normative legal acts in line with international standards; creating more severe sanctions for banking institutions that violate antitrust laws.

3. At the present stage of the first-order solution, the following aspects are required:

3.1. raising the level of capitalization of banking institutions that are in the process of reorganization;

3.2. increasing responsibility for violating the legal norms of participants in the processes of mergers and acquisitions;

3.3. improvement of legislative acts to ensure the fastest possible entry into the market of the newly established institution;

3.4. encouraging supervisors to revive mergers and acquisitions by introducing regulatory acts that would simplify the process of consolidation and help to minimize the process of consolidation.

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