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Mergers and Acquisitions in Banking Institutions with reference to State Bank of India

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ABSTRACT

The Banking sector has shown major changes in the past few years in terms of the Mergers and Acquisitions. Commercial banks are witnessing sweeping changes in the regulatory environment, huge growth in off balance sheet risk management of financial instruments, with the introduction of e-commerce, internet banking and significant consolidation of banks. All of these forces have made the Indian banking industry highly competitive. In this paper context, the study of performance of the banks after the merger assumes importance. This paper examines the impact of mergers on performance of Banking Institutions with reference to State Bank of India i.e.a comparison between pre and post-merger performance in terms of Operating Profit Margin, Net Profit Margin, Return on Assets, Return on Equity, Earning per Share, Debt Equity Ratio, Dividend Pay-out Ratio and Market Share Price has been made in case of SBI.

Keywords: Banking Sector, Efficiency, Merger and Acquisitions, Profitability

1. Introduction

Banking sector occupies a very important place in every economy and is one of the fastest growing sectors in India.Merger is a combination of two or more companies into one company or it may be in the form of one or more companies being merged into the existing companies. On the other hand, when one company takes over another company and to become an owner of that company is called as Acquisition. Every Merger and Acquisition must follow the legal procedure of mergers and acquisitions which is given by various Acts. Bank has no exception, they have to follow legal procedures of Mergers and Acquisitions,as directed by the Reserve Bank of India, SEBI, MCA, etc. Mergers and acquisitions are not a short-term process, it takes time to take decisions after examining all the aspects. The competition is intense, irrespective of all challengesfrom multinational players, domestic banks (both public and private) are rigorous in their pursuit of gaining competitive advantage.

Banking industry have to face competition, not only form banking industry within the country but also from international business giants, due toglobalisation, liberalisation, technological changes and other factors. The objectives of M&A are wealth maximisation in terms of synergy, strategic imperatives, capital market expectation, economies of scale, diversification, reduced earnings volatility, increased in domestic market and customer awareness.

"Mergers is the comparison of two or more companies in creation of a new entity or formation of a holding company. "Acquisition is the purchase of shares or assets another company to achieve a managerial influence not necessarily by mutual agreement" which is according to researchers (Ganghan, 2002). Chundai Chen & Findlay, 2003 &Jagersma, 2005).

"A merger or Amalgamation results in the combination of two or more companies into one, where in the merging entities lose their identities by being absorbed into the merger entity" according to author Ramaiya (1997).

2. Acts applicable to Banks in India

Various banks are formed for the various purposes, under different Acts. The private and public sector banks are subject to the provisions of the Banking Regulation Act, 1949, but the public sector banks are governed by their respective applicable statutes. On the other hand, co-operative banks are governed by the provisions of the Co-operative Societies Act of the respective State or by the Multi-State Co-operative Societies Act, as also by the provisions of the Banking Regulation Act. The Development Financial Institutions (DFIs), which were attract the provisions of those statutes while the DFIs structured as limited companies, subject to the provisions of the Companies Act.Both types of the DFIs are regulated and supervised by the RBI under the provisions of the RBI Act, 1934. Rural banks were created under the Regional Rural Bank (RRB) Act, 1976 and are regulated by the RBI but supervised by the NABARD, while the non-banking financial companies are subject to the provisions of the Companies Act and are regulated and supervised by the RBI.

3. Mergers in India

In general,mergers in India, have experienced an increase numbers in various sectors, especially after the New Economic Policy of the year 1991, which had opened the door for global markets. Banking Sector in India has witnessed many mergers during the decade, for various reasons such as Restructuring of Weak Banks; Economies of Scale; Expansion of Market; Business Consolidation etc. Looking into the history of mergers in banking sector in India, initially they have taken place as a measure to protect the interests of the customers of the weak banks.But subsequently a few mergers also taken place voluntarily after the Post Liberalisation period between various banks for several reasons.

The Indian economy, which is one of the fastest growing economies in the world, is poised to maintain its leading position, despite the global financial crisis and economic slowdown. India has managed to beat the global financial turmoil due to sound regulation, prudent financial supervision and proactive policies. India's growth is driven predominantly by domestic consumption, investment, good fiscal policy and the strong banking system, which had no direct exposure to the US sub-prime of assets mortgage or failure of banking institutions. During this period two mergers have taken place in Indian banking sector one between two profit-making Public-Sector Banks in the lines of consolidation and the other one was between two profit-making Private Sector Banks for the synergies of merger. In this context, the study of performance of the banks that have merged voluntarily assumes importance of sustainability and good governance.

4. Landmarks in Indian Banking Sector

- The Banking System of India was started in 1770.

- Indian Bank is First bank which is known as Bank of Hindustan.
- 1840: Bank of Bombay
- 1843: The Bank of Madras
- 1840: Bank of Calcutta
- 1921: All Banks which are above were merged and formed a new bank known as Imperial Bank of India.
- 1955: Imperial Bank was partially nationalized and was named as State Bank of India
- 1969: 14 banks were nationalized
- 1980: 6 more banks were nationalized
- 1993: The New Bank of India was merged with The Punjab National Bank

▪ Many small banks were set up in India during 1786 – 1969 which is known is initial Phase of banking or Phase I

▪ Nationalization, Regularization and Growth during 1969 – 1991 which is known as Phase II

▪ Liberalization and its aftermath are known as Phase III

Post liberalization regime Indian Banking Sector grown rapidly because of private banks. Which is because Government had initiated the policy of liberalization and licenses to the private banks.

5. Literature Review

Under this study, the researcher reviewed research papers for the purpose of providing a view into the work related to Merger and Acquisitions (M&As) in banking sector. With the M&As firms get benefit and growth internally and externally as well. By amalgamation, a firm can grow externally in the way of expansion, while internal growth in the form of effective services to the customers with good practices.

Aharon David Y et al., (2010), analysed the stock market bubble effect on Merger and Acquisitions, followed by the reduction of pre bubble and subsequent, the bursting of bubble seems to have led to further consciousness by the investors and provide evidence which suggests that during the euphoric bubble period investor take more risk. Merger of banks through consolidation is the significant force of change took place in the Indian Banking sector.

Dirk et al., (2009), explained the relationship between bank reputation after Merger and Acquisitions and its effects on shareholder's wealth. It is found in the study of "Bhaskar a Uday" et al., (2009) that banking sector witness of merger activities in India. Loosing of old customer and attraction of new customers,is a big problem to the banks. Then the acquiring firms and their merger happens which mainly focuses on the economies of scale, efficiency gain and address the need of communication and employee concern, and described the integration process was handled by professional and joint integration committee.

Integration road map was prepared as per schedule, inone of the cases of the Bank of Punjab acquired the Lord Krishna Bank, later on the Centurion Bank also took over by Bank of Punjab which later acquired by the HDFC Bank. This study regulates the link between communication, HR integration, management action and consequent contribution of post-merger success by conducted interview in a recent bank merger, in depth interviews work conducted in a recent merger. It was inferred that proactive communication, changes in

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organizational structure, and appropriate human resource integration would smoothen the journey towards successful integration.

Mantravadi Pramod & Reddy A Vidyadhar (2007)[i] evaluated, that the impact of merger on the operating performance of acquiring firms in different industries by using pre and post financial ratio to examine the effect of merger on firms. They selected all mergers involved in public limited and traded companies in India between 1991 and 2003, result suggested that there was little variation in terms of impact as operating performance after mergers. In different industries in India particularly banking and finance industry had a slightly positive impact of profitability on pharmaceutical, textiles, electrical and electronic sector, showed the marginal negative impact on operating performance. Some of the industries had a significant decline both in terms of profitability and return on investment and assets after merger.

Kumar and Bansal (2008)[ii], in their study "The Impact of Merger and Acquisitions on Corporate Performance in India" attempted to analyse whether the claims made by the corporate sector while going for M&As to generate synergy are being achieved or not in the Indian context. They did so by studying the impact of M&As on the financial performance of the outcomes in the long-run and compared and contrasted the results of merger deals with acquisition deals. The study used ratios and correlation matrix for analysis, and found that in many cases of M&As, the acquiring firms were able to generate synergy in the long run, which might have been in the form of higher cash flow, more business, diversification, cost cuttings and more.

Kumar (2009)[iii], in a work entitled "Post-merger Corporate Performance: An Indian Perspective" examined the post-merger operating profit of a sample of 30 acquiring firms involved in M&As activities during 1999 – 2002 in India. The study attempted to identify synergies, if any, resulting from mergers in Indian market. The study used accounting data to examine M&Arelated gains to the acquiring firms. It was found that post-merger profitability, assets turnover, and solvency of the acquiring firms showed no improvement when compared with pre-merger values.

6. Research Gap

Most of works in the above observations are recent trends in banking sectors, their policies and their framework but focus was not on the mergers and acquisitions in the banking sector. The present paper would go on study on the details of M&A mainly on the Indian Banking sector in post liberalisation period. The study will also be on the pre and the post-merger performance of banks.

7. Objectives of the Study

The objectives of the paper are to study the Mergers and Acquisitions of Banks from 1969 to till date. Evaluation of the bank's performance in terms of operating margin and net profitability, how was the performance of banks after merger.

8. Methodology

- **Data Collection:** For the purpose of evaluation of investigation data is collected from M&A of SBI bank. The financial and accounting data of banks is collected from banks annual reports to examine the impact of merger on financial performance of the banks and also from National stock exchange (NSE), Bombay stock exchange (BSE) & Money control.

- **Sample:**OnePublic Sector bank is taken as the sample bank to evaluate the impact of mergers and acquisitions.
- **Period of the Study:** To compare the performance of Banks, pre-merger and post-merger financial ratios are being taken.
- **Financial Aspects**: The performance of the Bank is taken in respect of the financial aspects such as Net Profit Margin, Operating Profit Margin, Return on Assets, Return on Equity. Debt Equity Ratio, Earning Per Share and Market Share Price.
- **Ratios**
  1. Gross Profit Margin Ratio : Gross Profit / Sales X 100
  2. Net Profit Margin Ratio: Net Profit / Sales X 100
  3. Operating Profit Margin Ratio : Operating Profit / Sales X 100
  4. Return on Capital Employed : Net Profit / Total Assets X 100
  5. Return on Equity : Net Profit / Equity Capital X 100
  6. Debt Equity Ratio : Total Debt / Total Equity X 100

Table 1. List of few Merger and Acquisitions (M&As) in Indian Banking Sector

Sl. No.	Name of the Transferor Bank	Name of the Transferee Bank	Date of Merger /Amalgamation
1	Bank of Bihar Ltd.	State Bank of India	November, 1969
2	National Bank of Lahore Ltd.	State Bank of India	February, 1970
3	Miraj State Bank Ltd	Union Bank of India	July, 1985
4	Lakshmi Commercial Bank Ltd	Canara bank	August, 1985
5	Bank of Cochin Ltd.	State Bank of India	August, 1985
6	Hindustan Commercial Bank Ltd	Punjab National bank	December, 1986
7	Traders Bank Ltd	Bank of Baroda	May, 1988
8	United Industrial Bank Ltd	Allahabad bank	October, 1989
9	Bank of Tamilnadu Ltd	Indian Overseas bank	February, 1990
10	Bank of Thanjavur Ltd.	Indian Bank	February, 1990
11	Parur Central Bank Ltd	Bank of India	February, 1990
12	Purbanchal Bank Ltd.	Central Bank of India	August, 1990
13	New Bank of India	Punjab National Bank	September, 1993
14	Bank of Karda Ltd	Bank of India	1993-1994
15	Kashi Nath Seth Bank Ltd.	State Bank of India	January, 1996
16	Bari Doab Bank Ltd	Oriental Bank of Commerce	April, 1997
17	Punjab Co-operative Bank Ltd.	Oriental Bank of Commerce	April, 1997
18	Bareilly Corporation Bank Ltd	Bank of Baroda	June, 1999

19	Sikkim Bank Ltd	Union Bank of India	December, 1999
20	Times Bank Ltd.	HDFC Bank Ltd	February, 2000
21	Bank of Madura Ltd.	ICICI Bank Ltd	March, 2001
22	ICICI Ltd	ICICI Bank Ltd	May, 2002
23	Benares State Bank Ltd	Bank of Baroda	June, 2002
24	Nedungadi Bank Ltd.	Punjab National Bank	February, 2003
25	South Gujarat Local Area Bank Ltd.	Bank of Baroda	June, 2004
26	Global Trust Bank Ltd.	Oriental Bank of Commerce	August, 2004
27	IDBI Bank Ltd.	IDBI Ltd	April, 2005
28	Bank of Punjab Ltd.	Centurion Bank Ltd	October, 2005
29	Ganesh Bank of Kurundwad Ltd	Federal Bank Ltd	September, 2006
30	United Western Bank Ltd.	IDBI Ltd.	October, 2006
31	Bharat Overseas Bank Ltd.	Indian Overseas Bank	March, 2007
32	Sangli Bank Ltd.	ICICI Bank Ltd	April, 2007
33	Lord Krishna Bank Ltd.	Centurion Bank of Punjab Ltd.	August, 2007
34	Centurion Bank of Punjab Ltd	HDFC Bank Ltd.	May, 2008
35	The Bank of Rajasthan	ICICI Bank Ltd	August, 2010
36	State Bank of Indore	State bank of India	August, 2010
37	ING Vyasa Bank	Kotak Mahindra Bank	November, 2014
38	All the 5 associates of SBI	State Bank of India	April, 2017
39	Bhartiya Mahila Bank (BMB)	State Bank of India	April, 2017
40	Vijaya bank and Dena Bank	Bank of Baroda	April, 2019
41	Punjab National Bank, Oriental bank of commerce and United bank of India	Punjab National Bank	August,2019
42	Canara Bank and Syndicate bank	Canara Bank	August,2019
43	Union Bank, Andhra Bank and Corporate Bank	Union Bank	August,2019
44	Indian Bank and Allahabad Bank	Indian Bank	August,2019

Table 2. Financial Performance of SBI

Year of Operations	**2016**	**2017**	**2018**	**2019**
Operating Profit Margin	-10.91	-14.23	-23.19	-14.14
Net Profit Ratio	6.06	5.97	-2.96	0.35
Return on Assets	0.42	0.38	-0.18	0.02
Return on Equity	6.89	6.69	-3.37	0.39

Earnings Per Share	12.82	13.15	-7.34	0.97
Debt Equity Share	14.24	15.08	15.79	16.89
Dividend Pay - out Ratio	20.28	20.11		
Share Price(NSE/BSE)	249.75	309.5	295.65	313.6

(Source: Compiled from the Financial Statements of Banks)

9. Conclusion

Mergers and Acquisition is a useful tool for the growth of banking business. There is no exception for the banking sector in India as well, which helps in the survival of the weak banks by merging into the strong bank. This study shows the impact of M&Ain the Indian Banking sector and SBI Bank with reference to recent merger of 5 banks have been taken for the study as sample to examine the as to whether the merger has led to a profitable situation or not. A comparison between pre and post-merger performance in terms of Operating Profit Margin, Net Profit Margin, Return on Assets, Return on Equity, earning per Share, Debt Equity Ratio, Dividend Pay-out Ratio and Market Share Price has been taken. In SBI there is no significant improvement in the performance after the merger as the merger was mainly in the interest of the public. In the initial stage, after merging, there may not be a significant improvement due to problems but later they may improve.

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