

IMPACT OF MERGER AND ACQUISITION ON PERFORMANCE OF SELECTED PUBLIC AND PRIVATE SECTOR BANKS IN INDIA

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Abstract

In Indian banking sector is one of the most important for improve growth of the country. This paper is for the check whether is any improvement in profitability and return on assets in post-merger and acquisition period of a bank. For this three public and 3 private bank select which are merged in 2016-2018 and prepare a report from that data. From overall study it indicates that merger is helpful for improvement of banking sector in India. Public bank do a very good performance after the merger as compare to private banks.

Keywords: merger and acquisition, banking sector, performance.

1. INTRODUCTION

1.1. Introduction of Indian Banking Sector

In India, India banks (public and private) credit growth was muted at 14.7% during 2013-2014 and Public Sector Banks Profitability saw a Significant Decline. The aggregated Profit after tax of public sector banks declined by 27% (Year on Year) to Rs. 370 Billion during FY2014 from Rs. 507 Billion during FY2013. Public Sector Banks Net Profitability declined to 0.50 in relation to average total assets during FY2014 vs. 0.78% during FY2013 and their return on Net Worth dropped to 9.1% FY2014 from 14.2% in FY2013. Public Sector Banks and Private Banks gross NPA% increase over the last one year from 3.3% to 3.9% as on March 2014. The increase in gross NPA% was due to higher fresh NPA generation rate (3.5-3.6% for Public Sector Banks in 2013-14, 3.4% in Q4, 2014 as against 3.1% in 2012-13). PSBs gross NPAs increased from 3.6% as on March 2013 to 4.4% as on March 2014. As for Q4, FY2014, Gross NPA% of PSBs declined by 30 basis points (bps) from December 31, 2013 levels. This reduction is due to higher recovery efforts towards the end of the financial year, higher write offs and sale of assets to asset reconstruction companies. Restructured advances of the Public Sector Banks remain at elevated levels of 6.2% as on March 31, 2014. Private sector banks were able to hold on good asset quality as reflected in their gross NPAs of 1.8% as on March 2014 (vs 1.9% as on December 2013)

1.2. The history of Indian Banking can be divided into Three Main Phases

Phase I (1786- 1969) - Initial phase of banking in India when many small banks were set up, Phase II (1969- 1991) - Nationalization, regularization and growth, Phase III (1991 onwards) - Liberalization and its aftermath With the reforms in Phase III the Indian banking sector, as it stands today, is mature in supply, product with banks having clean, strong and transparent balance sheets. The major growth drivers are increase in retail

credit demand, proliferation of ATMs and debitcards, decreasing NPAs due to Securitization, improved macroeconomic conditions, diversification, interest rate spreads, and regulatory and policy changes (e.g. amendments to the Banking Regulation Act).

1.3. Key points of the Banks Latest Performance and Outlook

1.3.1. Credit Growth Drops Marginally

Credit growth for the PSBs dropped from 15.3% in 2012-13 to 14% in 2013-14, while that for private sector banks increased from 16.6% to 17.8% with overall growth declined from 15.6% to 14.7% PSBs.

1.3.2. Earnings Deteriorate Sharply

Yield on advances for PSBs dropped by 40 basis points in FY2014 vs. FY2013, partly due to increase in Gross NPA%, partly due to reduction in base rate towards the end of 2012-13 as well as reduction in interest rates in selective segments (few banks, in a bid to gain higher growth in retail loans, reduced interest rates for housing & auto loans). However, this was offset by reduction in Cash Reserve Ratio (CRR), increase in G sec yields and marginal reduction in cost of funds, which led to only 10 basis points (bps) contraction in net interest margin (NIMs) to 2.5% in 2013-14 Reduction in NIMs by 10 bps and increase in credit cost by around 20 bps led to drop in PSBs profitability to 0.5% in relation to ATA, while the private sector banks continued to report robust profitability at 1.6% in relation to ATA. Lower yield on advances (9.7% for PSBs vs. 11.2% for private sector banks), lower non-interest income (0.9% vs 1.7%) and higher provisions (1.1% vs. 0.5 %,) were the key reasons for lower profitability of PSBs even as their operating expenses were moderate at 1.6% (as against 2.2% for private sector banks)

1.3.3. Asset Quality Slide Continues for PSBs

- Fresh NPA generation rate of PSBs increased to 3.5-3.6% in 2013-14 as against 3.1% in 2012-13 leading to increase in Gross NPA% to 4.4% as on March 31, 2014 from 3.6% the previous year. Gross NPA% of Private + Public Sector Banks increased to 3.9% from 3.3% in corresponding period.
- PSBs Standard restructured advances remained elevated at 6.2% as on March 31, 2014 Capitalization comfortable against the current regulatory norms.
- Banks started reporting capital adequacy as per Basel III norms since June 2013, Tier 1 capital of PSBs was around 8.6% as on March 31, 2014 as against the required Tier 1 capital of 6.5%, while that of private sector banks was well above the norms around 12.8%.
- Operating profits as % of Net NPAs for PSBs was 90% during FY2014 as against 130% during FY2013.

1.4. Scenario of Merger in Banking Sector

In worldwide banking sector has shown major turmoil in the past few years in merger and acquisitions. Some deregulations are the main three routes: Dismantling of interest rate control, Removal of barriers between banks and other financial intermediaries, and lowering of entry barriers. Its leads to disintermediation, Investor wants high returns, Price competition, fallen margins, and competition across geographies forcing banks to look for new ways to boost revenue. For that types of issue merger are very much useful for scale-economies, geographical diversification, lower costs branch and staff rationalization, cross border expansion and market share concentration. The G20 new Basel II norms have also led banks to consider Mergers. Like all business entities, banks want to safeguard against risks, as well as exploit available opportunities indicated by existing and expected trends. M&As in the banking sector have been on the rise in the recent past, both globally and in India. In this backdrop of emerging global and Indian trends in the banking sector, this article illuminates the key issues surrounding M&As in this sector with the focus on India. It seeks to explain the motives behind some M&As that have occurred in India post-2000, analyze the benefits and costs to both parties involved and the consequences for the merged entity. M&As that have

happened post-2000 in India to understand the intent (of the targets and the acquirers), resulting synergies (both operational and financial), modalities of the deal, congruence of the process with the vision and goals of the involved banks, and the long term implications of the merger. The article also analyses emerging future trends and recommends steps that banks should consider, given the forecasted scenario.

2. LITERATURE REVIEW

- Ms. S. Revathy (Dec,2011)Based on the trends in the banking sector and the insights from the cases highlighted in this study, one can list some steps for the future which banks should consider, both in terms of consolidation and general business. Banks need to take advantage of this fast changing environment, where product life cycles are short, time to market is critical and first mover advantage could be a decisive factor in deciding who wins in future. Post-M&A, the resulting larger size should not affect agility.
- Srinivasan R. (2011) Post-M&A, the resulting larger size should not affect agility. The aim should be to create a nimblegiant, rather than a clumsy dinosaur. At the same time, lack of size should not be taken to imply irrelevance as specialized players can still seek to provide niche and boutique services.
- Mr. Chirag Aggarwal (Nov. 2012) Mergers and Acquisitions is the only way for gaining competitive advantage domestically and internationally and as such the whole range of industries are looking to strategic acquisitions within India and abroad. In order to attain the economies of scale and also to combat the unhealthy competition within the sector besides emerging as a competitive force to reckon with in the International economy. Consolidation of Indian banking sector through mergers and acquisitions on commercial considerations and business strategies – is the essential pre-requisite.
- Devarajappa S. (Sept. 2012) Merger is the useful tool for growth and expansion in Indian Banking Sector. It is helpful for survival of weak banks by merging into larger bank. This study shows that impact of merger on financial performance of Indian Banking sector.
- Kanchan Jatkar (March 2012)Based on the trends in the banking sector and the insights from the cases highlighted in this study, one can list some steps for the future which banks should consider, both in terms of consolidation and general business of consolidation and general business. Firstly, banks can work towards a synergy based merger plan that could take shape latest by 2009 end with minimization of technology-related expenditure as a goal. There is also a need to note that merger or large size is just a facilitator, but no guarantee for improved profitability on a sustained basis. Hence, the thrust should be on improving risk management capabilities, corporate governance and strategic business planning.
- M Jayadev (2012) Voluntary mergers demonstrating market dynamics are very few. We strongly support the view that Indian financial system requires very large banks to absorb various risks emanating from operating in domestic and global environments. We argue that the challenges of free convertibility, Basel-II environment, widening of financial services activity, and need for large investment banks are the prime drivers of future consolidation. More voluntary mergers are possible provided the benefits of mergers are derived by all the stakeholders of the banks.
- ShailShakya (2014) Indian PSBs have long been burdened with the responsibility of development banking through mobilizing deposits at the countryside and providing finance to agriculture and small scale industries at subsidized rates. It is time to marry the social responsibility of these banks with proper commercial orientation so that they can survive and prosper in an environment of high growth, competition and risks.

2.1. NEED FOR THE STUDY

In recent time period merger are most important factor for the scale-economies, geographical diversification, lower costs branch and staff rationalization, cross border expansion and market share concentration. so much research are already done on financial performance of bank in India but very less study are done on the research related to merger impact on public and private sector banks in India

3. RESEARCH METHODOLOGY

3.1. Research Objectives

To analyze the impact of merger on public and private sector Banks. To find the effect of merger on equity shareholder's wealth. To know the pre and post effect of merger on Public and private sector banks.

3.2. Research Design

In this study I use descriptive Research Design as this study will assist the decision maker in determining, evaluating and selecting the best course of action to take in a given situation.

3.3. Selection of Sample and Sources of Data

I use six banks data for the study of this research. Three public sector bank and 3 private sector bank. Whose merger is done in the period of 2016-2018. Public Sector Banks are IDBI bank, Indian Overseas Bank and State Bank of India. Private Sector Banks are Federal bank, ICICI bank and HDFC bank. For this research data are collected from the websites, journals, Books.

4. Data Analysis

4.1. Public sector banks

Table 1: pre-merger selected public sector banks

Ratio analysis	IDBI Bank	Indian overseas bank	State bank of India
Adjusted cash margin	10.55	16.69	13.06
Net profit margin	7.21	16.44	11.21
Return on long term fund (%)	87.61	107.40	97.89
Return on net worth (%)	9.21	28.55	15.94
Return on assets	88.04	58.32	525.25
Post-merger of selected public sector banks			
Adjusted cash margin	8.73	14.49	12.81
Net profit margin	7.54	17.94	11.65
Return on long term fund (%)	120.38	146.37	86.83
Return on net worth (%)	10.72	25.35	13.72
Return on assets	121.72	89.15	776.48

4.2. Interpretation

From the above table we can interpret that Net Profit Margin is increases after the merger and its 7.21 to 7.54 respectively. It indicates that merger is profitable for the IDBI bank because of increase in Net Profit Margin. Return on Long Term fund also got a very good performance after the merger so post-merger impact is profitable for IDBI Bank. 87.61 to 120.38 pre and post-merger impact are measured in IDBI Bank. Return on Net Worth and Return on Assets also do a good performance after the merger. Return on Net worth are 10.72 from 9.12 after the merger and Return on Assets are 88.04 to 121.72 after the merger. So, from all this data IDBI bank is perform well after merger. For the Indian overseas Bank adjusted cash margin 16.69, Net Profit Margin 16.44, Return on Long Term Fund is 107.40, Return on net worth 28.55, return on assets is 58.32 this all are pre-merger data where Post merger data are adjusted cash margin 14.79, Net Profit Margin 17.94, Return on Long Term Fund is 146.37, Return

on net worth 25.35, return on assets is 89.15. From that data its clearly indicate that after the merger profitability is increases after the merger. Same in State Bank of India adjusted cash margin 13.06, Net Profit Margin 11.21, Return on Long Term Fund is 97.89, Return on net worth 15.94, return on assets is 525.25 is a pre-merger data where after the merger data is adjusted cash margin 12.81, Net Profit Margin 11.65, Return on Long Term Fund is 86.83, Return on net worth 13.72, return on assets is 776.48.

4.3. Private sector banks

Table 2: Pre-merger selected private sector banks

Ratio analysis	Federal Bank	ICICI bank	HDFC Bank
Adjusted cash margin	15.05	17.55	23.11
Net profit margin	13.64	14.12	15.55
Return on long term fund (%)	89.71	56.24	60.06
Return on net worth (%)	22.99	14.33	22.73
Return on assets	146.02	249.55	169.24
Post-merger of selected public sector banks			
Adjusted cash margin	13.80	11.81	15.01
Net profit margin	14.05	10.51	12.82
Return on long term fund (%)	55.12	62.34	62.34
Return on net worth (%)	9.39	8.94	13.83
Return on assets	229.53	417.64	324.38

4.4. Interpretation

From the above table we can interpret that Net Profit Margin is increases after the merger and its 13.64 to 14.05 respectively. It indicate that merger is profitable for the Federal Bank because of increase in Net Profit Margin. Return on Long Term fund also got a very good performance after the merger so post-merger impact is profitable for Federal Bank. Return on Net Worth and Return on Assets also do a good performance after the merger. Return on Net worth are 22.99 from 9.39 after the merger and Return on Assets are 146.02 to 229.53 after the merger. So, from all this data Federal Bank is performing well after merger. For the ICICI Bank adjusted cash margin 17.55, Net Profit Margin 14.12, Return on Long Term Fund is 56.24, Return on net worth 14.33, return on assets is 549.55 this all are pre-merger data where Post merger data are adjusted cash margin 11.81, Net Profit Margin 10.51, Return on Long Term Fund is 62.34, Return on net worth 8.94, return on assets is 417.64. From that data its clearly indicate that after the merger profitability is increases after the merger. Same in HDFC Bank adjusted cash margin 23.11, Net Profit Margin 15.55, Return on Long Term Fund is 60.06, Return on net worth 22.73, return on assets is 169.24 is a pre-merger data where after the merger data is adjusted cash margin 15.01, Net Profit Margin 12.82, Return on Long Term Fund is 62.34, Return on net worth 13.83, return on assets is 324.38.

PUBLIC SECTOR BANKS**4.5.IDBI Bank**

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	443.0234	1	443.0234	0.157222	0.702094	5.317655
Within groups	22542.53	8	2817.817			
Total	22985.56	9				

4.6. Interpretation

In IDBI Bank the P-Value is 0.702094 and F value is 0.157222its indicate that there is a positive impact of merger on banks. This impact measurement of IDBI pre and Post-merger.

4.7. INDIAN OVERSEAS BANK

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	438.244	1	443.0234	0.181913	0.680979	5.317655
Within groups	19272.68	8	2409.085			
Total	19710.92	9				

4.8. Interpretation

In overseas bank the P-value is 0.680979 and F-value is 0.181913,its indicate that there is positive impact on merger on bank.

4.9.STATE BANK OF INDIA

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	5671.066	1	443.0234	0.070184	0.797768	5.317655
Within groups	646425.5	8	80803.19			
Total	652096.6	9				

4.10. Interpretation

In overseas bank the P-value is 0.797768 and F-value is 0.070184,its indicate that there is positive impact on merger on bank.

PRIVATE SECTOR BANKS**4.11.Federal bank**

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	118.88704	1	118.887	0.01931	0.89293	5.31766
Within groups	49265.53056	8	6158.19			
Total	49384.4176	9				

4.12.Interpretation

In private bank also impact is positive. P-value 0.89293 and F-value is 0.01931.after the merger bank improve their performance.

4.13. ICICI Bank

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	2545.43025	1	2542.43	0.12124	0.73668	5.31766
Within groups	167765.6626	8	20970.7			
Total	170308.0928	9				

4.14.Interpretation

In ICICI Bank also do great performances after the merger P-Value 0.73668 and F-Value is 12124.it indicate that performance of ICICI Bank is good after the merger.

4.15. HDFC Bank

ANOVA						
Source of variation	SS	df	MS	F	P-value	F crit
Between groups	1895.85361	1	1895.854	0.169217	0.691608	5.317655
Within groups	89629.47	8	11203.68			
Total	91525.32361	9				

4.16. Interpretation

HDFC Bank is also performing well after merger. HDFC Bank has a high impact with the merger P Value is 0.691608 and F Value is 0.169217.

5. Conclusion

In Indian Banking Sector merger and Acquisition is the useful tool for the growth. It's helpful for the weaker bank to survive and make it large with the merger. This Study is shown the impact of Merger and Acquisition in the public and private banking sector particular in India. For that study use a various ratio analysis and also do an ANOVA for measurement of impact. Compare to public sector private sector are slightly decline because of merger and acquisition. Overall impact of merger and acquisition is positive on the Indian Banking Sector. So, It can be concluded that merger between the two banks is beneficial for Indian Bank

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