Pre & Post-Merger FinancialPerformance of Banks: An IndianPerspective

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ABSTRACT:

Mergers and Acquisitions are the important strategy for the growth and for enhanced competitiveness.In the Indian banking industry it is used for financial restructuring also.In the present study, an attempthas been made to assess the resultant effect of mergers and acquisition on two banks namely, Oriental Bank of Commerce and IDBI bank with respect to their financial performance on the basis of a set of ten financial parameters.Through literature review it comes to know that most of the work done high lightened the impact of merger and acquisitions on different financial aspects of acquiring bank. The relevant data collected was analyzed and tested with the help of paired‘t’ test. The analysisrevealed that there was significant improvement in some of the financial parameters in both the cases.However, some parameters have shown decay in the financial status of the corresponding financial indicators in the respective bank. This performance being tested on the two basis, one is pre merger and second is post merger performance.

KEYWORDS

Merger & Acquisition, Indian Banks, Paired‘t’ test, Financial Performance and FinancialIndicators

INTRODUCTION

In the globalized economy, Mergers and Acquisitions (M&As) act as a catalyst tool for the growth and expansion of the business. Merger creates synergy and economies of scale. Business entrepreneurs are using Mergers and Acquisitions worldwide as a strategy for achieving larger business size, increased market share, reduced cost, faster growth, and synergy for becoming more competitive through economies of scale.

The Banking system of India was started in 1770 and the first bank was the Indian Bank known as the Bank of Hindustan. Later on some more banks like the Bank of Calcutta-1806 (Bank of Bengal), Bank of Bombay-1840 and Bank of Madras-1843 were established under the charter of British East India Company. History of mergers in Indian banking industry was started in 1921 with the merger of Bank of Bengal, Bank of Bombay and the Bank of Madras and formed the Imperial Bank of India, which is now known as State Bank of India.

The economic reforms brought a change in the competitive landscape of Indian banking industry compelling banks to go for mergers with the objective of restructuring in order to enhance the profitability and competitive strength. In the past, mergers in banking sector were initiated by regulators to protect the interest of depositors of weak banks. But it is now expected that market led mergers may gain momentum in the coming years.

The advantages stemming from mergers and acquisitions can be evaluated by the financial performance of the firm. Financial performance evaluation provides a relative basis for comparing a company with itself over a period of time. Keeping all these points in mind, in the present study researcher has tried to assess the impact on the acquiring bank's financial performance after the acquisition with the help of financial parameters like Net Profit Margin, Return on Net Worth, Return on Capital Employed, Total Assets Turnover Ratio, Fixed Assets Turnover Ratio, Total Debt/ Equity Ratio, Current Ratio, Quick Ratio, Book Value Per Share and Earning Per Share.

The paper is organized in five sections. Section I presents introduction to the topic. Objectives of the study are discussed in Section II. Section III presents research methodology. Analysis of data is discussed in section IV. Finally concluding observations of the study are presented in section V.

RESEARCH OBJECTIVES

The main objective of this study is to investigate the pre and post merger financial performance of acquiring bank with the help of following parameters: Net Profit Margin, Return on Net Worth, Return on Capital Employed, Total Assets Turnover Ratio, Fixed Assets Turnover Ratio, Total Debt/ Equity, Current Ratio, Quick Ratio, Book Value, Earning Per Share. The results of the study would serve as a possible aid for policy makers in banking sector and in the Government.

RESEARCH HYPOTHESIS

- H0 (Null Hypothesis) = There is no significant improvement in the post merger financial position.
- H1 (Alternative Hypothesis) = There is significant improvement in the post merger financial position.

METHODS AND MATERIALS

The research is confined to two purposively selected banks that is IDBI bank in private sector and Oriental Bank of Commerce in public sector. The data of different financial indicators to study the pre and post merger performance of banks was referred to website of rbi.org.in, cmie.com etc. The period of study as under:

1. Oriental Bank of Commerce
    a. Pre merger period 1999 to 2003
    b. Post merger period 2005 to 2009
2. IDBI Bank
    a. Pre merger period 2001 to 2005
    b. Post merger period 2007 to 2011

To verify the underlying hypothesis and achieve the desired objectives, necessary statistical tool mainly Paired‘t’ test was used where

$$t = \frac{\bar{d} - 0}{\& / \sqrt{n}} \quad \text{for n – 1 degree of freedom}$$

$\bar{d}$ = Mean of the differences between Pre and Post observations

& = Standard Deviation

n = Number of Pre and Post Years

RESULTS AND DISCUSSION

Pre-merger and Post-merger Ratios of Oriental Bank of Commerce

	Mean		Std. Deviation		t-Values	Sig.
	Pre	Post	Pre	Post		
Net Profit Margin (%)	9.7660	13.6080	1.9779	3.9195	-1.780	0.150
Return on Net Worth (%)	20.3580	15.3320	4.1028	5.1582	2.391	0.075
Return on Capital Employed	9.8820	8.5480	4.4939	0.7103	0.677	0.535
Total Assets Turnover Ratio	.1200	.0860	0.0000	0.0089	8.500	0.001
Fixed Assets Turnover Ratio	9.7300	5.7480	.1012	1.0976	8.373	0.001
Total Debt/Equity Ratio	15.8120	13.4400	1.2387	2.7862	1.708	0.163
Current Ratio	.0360	.1500	.0055	.1464	-1.678	0.169
Quick Ratio	19.7920	13.9140	6.6169	1.5452	2.548	0.063
Book Value Per	84.9360	225.7520	14.2769	44.9206	-7.309	0.002

Share(Rs)						
Earning Per Share	15.8660	26.6740	4.9112	10.0171	-2.542	0.064

Pre-merger and Post-merger Ratios of IDBI Bank Ltd.

	Mean		Std. Deviation		t-Values	Sig.
	Pre	Post	Pre	Post		
Net Profit Margin (%)	7.2120	7.4720	1.7510	1.1248	-.507	0.639
Return on Net Worth (%)	7.1540	11.5600	1.2778	1.2463	-7.097	0.002
Return on Capital Employed	12.5360	8.2420	5.4289	0.4300	1.717	0.161
Total Assets Turnover Ratio	.0960	.0780	0.0336	0.0045	1.152	0.313
Fixed Assets Turnover Ratio	4.980	.8840	2.7646	1.1084	2.970	0.041
Total Debt/Equity Ratio	3.6300	13.4820	3.5845	5.0239	-9.600	0.001
Current Ratio	2.7400	0.0500	2.9494	0.0354	2.060	0.108
Quick Ratio	8.2040	16.3740	2.4138	7.9999	-1.872	0.135
Book Value Per Share (Rs)	105.7840	104.9620	20.8081	16.7428	0.051	0.962
Earning Per Share	7.8100	12.3200	1.6362	3.2324	-2.366	0.077

The time series data in respect of two banks under study namely Oriental Bank of Commerce and IDBI bank was further subjected to segregation to pre and post periods. Each of the pre and post period contained the different financial indicators namely,NetProfitMargin, Return on Net Worth, Return on Capital Employed, Total Assets Turnover Ratio, Fixed assets Turnover Ratio, Total Debt/Equity, Current Ratio, Quick Ratio, Book value per share and Earning Per Share. The periodicity of each was of five years. Necessary statistical analysis was carried out to compare pre and post period observations and the results are summarized in table 1 and table 2 respectively for Oriental Bank of Commerce and IDBI bank.

ORIENTAL BANK OF COMMERCE

It is observed in table 1 that mean of net profit margin has gone up in the post period but statistically not found to be significant as‘t’ value was -1.780. This indicates that although non-significant but indication of higher net profit margin due to merger. As far as return of net worth is concerned there is decline in the post merger period and statistically non- significant. It indicates that return on net worth has negative effect of merger for the reasons best known to bank itself (t = 2.39). Similar patter is observed on return on capital employed also witht = 0.677. the total assets turnover ratio which is one of the importantfinancial indicators to measure the efficiency/ profitability of the banks, has also gone down and difference between pre and post merger has been found to be highly significant (t = 8.5, P< 0.01) almost similar pattern is observed in the fixed assets turnover ratio with ‘t’ = 8.37, P< 0.01. It indicates that the merger has not given much impact for the development of the bank with regard to return on net worth, return on capital employed, total assets turnover ratio and fixed assets turnover ratio, quick ratio are also showing non-significant effect of merger in the case of Oriental Bank of Commerce.If we consider the book value per share are clear indication about the improvement due to merger with highly significant‘t’ value of -7.31, P < 0.01. Lastly the earning per share although has gained due to post merger effect but due to higher variability in the data on post mergerseries the difference is found to be not so statistically significant. It could be safely said that if longer period is studied earning per share may also show significant effect of merger in case of Oriental Bank of Commerce.

IDBI BANK

Table 2 gives the analysis of data pertaining to IDBI bank to measure the impact of merger on various financial indicators under study. The net profit has shown a slight improvement in post merger period but not statistically significant with‘t’ value -0.507. However the return on net worth has shown a comparatively better picture with a very highly significant increase. (t = 7.1, P < 0.01) this is not in case of Oriental Bank of Commerce. It is worth noting that return on capital employed has gone down as is evident in table 2. The total assets turnover ratio along with fixed assets turnover ratio has shown decline during the post merger period with highly significant difference for the latter one.

Now let us discuss an important indicator that is total debt/ equity. It is interesting to note that this variable has shown as highest growth during the post merger period with‘t’ value of -9.6, P < 0.01. The analysis suggested that some of the other important financial indicator like current ratio and book values have also gown down although statistically non-significant. One of the important feature of this analysis was observed that quick ratio and earning per share are quantum wise increasing in the mean values but tested with‘t’ test they are non-significant effects. The overall analysis of the IDBI bank suggested that except return on net worth and total debt/equity all are showing much impact of merger.

CONCLUDING OBSERVATIONS

As per foregoing discussion it can be stated that Mergers and Acquisitions are considered as a useful tool for growth and development among all the sectors which is true for banking sector also. It is helpful to create synergy and competitive advantageor for the survival of weak banks by merging into larger bank. In the present investigation two cases were examined.

After the merger it was observed that various financial al indicators of Oriental Bank of Commerce like net profit margin, current Ratio, book value per share and earning per share have shown significant improvement others have declined in magnitude and could not sustain the current level. In case of IDBI bank net profit margin, return on net worth, total debt/equity ratio, quick ratio and earning per share have shown significant improvement but rest of the indicators (return on capital employed, total assets turnover ratio, fixed assets turnover ratio, current ratio and book value per share)have not shown any significant improvement.

So result concluded here that the size of the bank may increase, but improvement in the financial position is not guaranteed. It is suggested that more number of banks were considered for analysis for generalization of the impact of the merger on the banks.

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