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Impact of Recent Banking Mergers – An Empirical View

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Abstract

This paper studies merger/consolidation of banks in India and the consequences . PNB had been a strong bank with an uninterrupted record of profits, but it suffered a net loss of ₹96 crore in 1996, following the merger. It had to face several problems and litigation relating to absorbing the staff of New Bank of India in its stream. It reportedly took PNB five years and more to get over the merger effect. SBI Merger and Lessons The recent merger of five ABs with SBI is hailed as path-breaking. Three of the ABs were stock-listed entities in which SBI had dominant holdings, while the remaining two were wholly owned by it. Known once as the "seven sisters," the ABs had been established by princely states before the country's independence to serve local populations. These came under the fold of SBI after the government passed the State Bank of India (Subsidiary Banks) Act in 1959. Thus, State Bank of Bikaner and Jaipur (SBBJ) (which was a merger of banks belonging to two princely states, Bikaner and Jaipur) came into being as SBI's subsidiary in 1963. Bank of Indore, originally established by Maharaja Tukoji Rao Holkar in 1920, became State Bank of Indore.

Key words: RBI, Merger, SBI, PNB, Narasimham Committee.

Introduction

The combined headcount of employees at ABs, about 70,000, is a third of SBI's aggregate strength, which is now the fifth largest employer in India. Integrating this huge number and deploying them productively would pose major issues. Besides the bloated employee costs, the pension and retirement benefits would make a large dent on SBI's profitability for several years. SBI is said to be evaluating the issue of rationalising the branch network post-merger. Early estimates might reveal that over 1,000 branches may need to be combined, or operations rationalised/relocated. There are challenges in enhancing skill levels of employees of erstwhile ABs who had so far had a regional focus with limited exposure. While SBI has some bandwidth to face these and other challenges due to its trained executive pool and large capital resources, absorbing more than one bank at the same time would be a nightmare for other PSBs. Merger of PSBs It is well known that the consolidation exercise of PSBs has moved to the front pages of newspapers following their mounting non-performing assets (NPAs) and the pressures for infusing additional capital faced by the government. In the process, there is a visible sense of urgency to rush through a process that should have been spaced out in an orderly and well-thought-out manner from the time it was mooted more than two decades ago. The excessive bad loans in some PSBs have not been a new phenomenon. The public sector Indian Bank, for example, was once saddled with a record loss of ₹1,336 crore in 1996, a result of faulty credit decisions in the past. There were suggestions to restrict Indian Bank as a "narrow bank." The bank, however, did a remarkable turnaround in three years and bounced back to sustained profitability.

Objective:

This paper intends to explore impacts of merger / acquisition in banks with government as the biggest shareholder of over 25 banks had to provide capital for them

There have been several learned discussions recently, that the high level of NPAs of PSBs is attributable to the general business cycle—the downswing in economic climate following the boom years of 2007–08. PSBs are faulted for their overzealous involvement in lending to the infrastructure sector following the vacuum created by the absence of development banks, without caring to build proper risk assessment and project monitoring capabilities on their own. By March 2015, NPAs in the infrastructure sector of PSBs were 22.8% of their aggregate problem loans. As pointed out by former RBI Governor Raghuram Rajan, a large chunk of NPAs at PSBs relate to projects that are indeed viable. These projects have remained incomplete for several extraneous reasons, such as problems in land acquisition and environmental clearances, which are hopefully being addressed by the concerned ministries. This is bound to improve the risk rating of NPAs in the period ahead. While the bad loans have resulted in negative credit growth in PSBs and a general mood of risk aversion, the banks have, at the same time, stepped up personal lending activity, specifically housing loans. PSBs' personal loan growth today has approached that of the private sector banks. The exercise of consolidating PSBs should therefore be based on a sound analysis of every PSB, a granular analysis of its assets and liabilities, sector-wise loan exposures, security back-up, common loans among PSBs, etc. A key factor to consider is whether the merger of any two PSBs would result in substantial value addition in the combined entity, or result in value diminution. Just the large size of a combined balance sheet cannot be a conclusive indicator. It is also worth asking as to whether PSB mergers would make better sense once there is progress in resolving the current unconscionable levels of NPAs.

Conclusion

An independent assessment of the scope for mergers in PSBs should look into whether there are alternatives to consider for the long-term soundness of "weak" PSBs, which could also lessen the pressure for additional capital. For a merger or any other restructuring option, PSBs face the foremost challenge of an acute talent deficit and absence of the right people in sufficient numbers. Almost every PSB on the merger radar lacks talented personnel to effectively manage even existing operations. Several case studies have shown that merger announcements trigger confusion, anxiety and insecurity in staff, leading to slowdowns in business. Weak talent management and poor communications often exacerbate these challenges. PSBs need leaders with considerable vision, maturity, strong operational knowledge, along with persuasive skills and the ability to cobble a diverse team to effectively implement a blueprint. The short tenure of senior leaders in PSBs comes in the way of launching any strategic initiative. Suggestions on bringing the right talent to PSBs at various levels and ensuring long tenures for the best personnel have remained on paper.

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