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MERGERS & ACQUISITIONS IN BANKING SECTOR: ANALYSIS OF FINANCIAL PERFORMANCE & THEIR EFFICIENCY OF ACQUIRING BANKS

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Abstract:

This research paper delves into mergers and acquisitions (M&A) in the banking sector, emphasizing financial performance, operational efficiency, and wealth implications for acquiring banks. Examining profit statements, dividend ratios, and motivations driving M&A, including market consolidation and regulatory shifts, the study evaluates short and long-term effects on key indicators. Efficiency gains are assessed using metrics like the impact on dividend ratios is explored in the context of shareholder wealth. Historical evolution in the Indian banking sector, shaped by economic reforms and policy changes, is considered, along with the regulatory framework governed by the Reserve Bank of India and the Competition Commission of India. The research identifies motives such as economies of scale, cost efficiency, and strategic positioning, revealing nuanced variations in domestic and cross-border transactions. Insights on the impact of M&A on financial performance, efficiency, and shareholder wealth are drawn, with determinants of success including due diligence, post-merger integration, and organizational culture alignment. This condensed abstract provides valuable insights for investors, policymakers, and banking executives.

keywords - *Banking Mergers, Financial Performance, Regulatory Framework, Strategic Integration*

Introduction:

The paramount objective for any corporation is to maximize profits and to reach the markets. Businesses can pursue internal growth by innovating and developing new products. Additionally, they can opt for external growth strategies, such as mergers and acquisitions (M&A), to propel their expansion. M&A strategies have garnered immense popularity across diverse sectors due to the increasing levels of privatization, globalization, and liberalization observed in many countries worldwide. Mergers and acquisitions (M&A) are seen as a faster and more efficient way to enter new markets and increase market share. Currently, the Indian banking industry faces challenges such as increasing net losses, rising non-performing assets (NPAs), growing operating costs, declining net worth, and fierce competition between public and private sector banks. To address these issues, the Indian government has encouraged M&A in the banking sector. This has resulted in a shift from many small banks to a smaller number of larger banks. It has improved operational efficiency, reduced financial risks, provided access to specialized services, enhanced lending capacity, and expanded financial inclusion services. M&A in banking can stimulate economic growth by increasing capital flow, returns to shareholders, investments in research and development, and creating growth opportunities. Consequently, it significantly impacts the country's GDP growth. However, banks face challenges during the M&A process that can affect their efficiency. Therefore, it is essential to assess various parameters to gauge the efficiency of banks before and after M&A. These strategic moves empower companies to position themselves competitively on a global scale. Nevertheless, it is worth noting that there have been instances where mergers and acquisitions have been undertaken primarily to enhance a company's reputation, rather than solely for value-maximizing purposes.

Significance of the Study:

This research holds significant implications for various stakeholders. Banking professionals can gain insights into the motives behind M&A activities & the factors contributing to their success, facilitating informed decision-making. Academics can contribute to the existing body of knowledge surrounding M&A in banking, The present study takes into consideration six years. 3 years prior to M&A and 3 years post M&A as the M&A took place in the year 2020. In this study the effect of inflation has not been considered at the time of analyzing the efficiency of selected banks in the pre and post M&A of banks. fostering further research & exploration in this evolving field. Ultimately, the study aims to provide valuable insights that contribute to the sustainable development & resilience of the banking sector in the ever-changing economic landscape.

Historical Context & Regulatory Framework of Mergers & Acquisitions in Indian Banking:[1]

Evolution of Mergers & Acquisitions in Indian Banking: The historical evolution of mergers & acquisitions in the Indian banking sector traces a transformative journey from 1921.

Normal merger and amalgamation (Section 230-232): This involves the approval of a scheme of arrangement or compromise by the National Company Law Tribunal (NCLT) after obtaining the consent of the shareholders, creditors, and other stakeholders of the companies involved. The scheme must also be filed with the Registrar of Companies (ROC) and other relevant authorities.

[1] India: Mergers And Acquisitions In The Indian Banking Sector - Mondaq.
https://www.mondaq.com/india/shareholders/1263072/mergers-and-acquisitions-in-the-indian-banking-sector.
2.Mergers & Acquisitions in Indian Banking Sector: Regulatory Issues ....
https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2399288.
3.Mergers and Acquisitions in Indian Banking Sector: Pre-Post Analysis of .... https://www.iosrjournals.org/iosr-jbm/papers/Vol17-issue3/Version-2/A017320109.pdf.

Section 230 allows a company to propose a scheme or a mode for compromise or arrangement with its creditors or its members, or both, when the company aims to restructure or reorganize its debt in order to resolve a financial crisis. The scheme or the mode has to be approved by the National Company Law Tribunal (NCLT) and the majority of the creditors or members, as the case may be.

Section 231 empowers the NCLT to supervise the implementation of the scheme or the mode approved under section 230, and to give directions or make modifications as it may consider necessary for the proper implementation of the scheme or the mode.

Section 232 lays down the procedure for merger or amalgamation of two or more companies, which involves filing of a draft scheme with the NCLT, sending notices and disclosures to the creditors, members, and other stakeholders, holding meetings to obtain their consent, and obtaining the sanction of the NCLT for the scheme. The section also provides for certain exemptions and relaxations for certain classes of companies, such as small companies, holding and subsidiary companies, and government companies.

Examination of object clauses: The parties must examine the object clauses of their respective memorandum of association to ensure that they have the power to undertake the proposed transaction.

Intimation to stock exchanges: If the parties are listed on any stock exchange in India, they must intimate the stock exchange about the proposed transaction and comply with the disclosure requirements under the SEBI Regulations.

Approval of the draft merger proposal by the respective boards: The parties must obtain the approval of their respective boards of directors for the draft merger proposal and the share exchange ratio, if any.

Obtaining the necessary approvals: Obtain the necessary approvals from the RBI, the CCI, the SEBI.

Application to NCLT: The parties must file an application to the relevant NCLT for sanctioning the scheme of arrangement under the Companies Act, 2013. The NCLT may direct the parties to convene meetings of their shareholders and creditors to seek their approval for the scheme.

Dispatch of notice to shareholders and creditors: The parties must dispatch the notice of the meeting, along with the scheme of arrangement and the explanatory statement, to their shareholders and creditors at least 21 days before the date of the meeting.

Holding of meetings of shareholders and creditors: The parties must hold the meetings of their shareholders and creditors and obtain their approval for the scheme by the requisite majority. The scheme must be approved by at least 75% of the shareholders and creditors present and voting at the meeting.

Petition to NCLT for confirmation and passing of NCLT orders: The parties must file a petition to the NCLT for confirming the scheme of arrangement and seek its sanction. The NCLT may approve the scheme with or without modifications, or reject it, after considering the objections, if any, raised by the shareholders, creditors, or any other interested parties.

Filing the order with the registrar: The parties must file the certified copy of the NCLT order with the registrar of companies within 30 days of the receipt of the order. The scheme becomes effective from the date of filing of the order with the registrar.

Pre and Post analysis of Three Merged Banks: -

1. Canara Bank and Syndicate Bank:[2]

pre-merger profit statement of both banks. The profit statements and dividend reports of Canara Bank and Syndicate Bank in 2018, 2019, and 2020 are as follows:

1. Canara Bank (Profit statement):

Bank (Profit+/Loss-)	Canara Bank
2018	Rs. - 4,222.24 Crore
2019	Rs. – 552.02 Crore
2020	Rs. +1,010.87 Crore

Dividend Report:

Dividend	Canara Bank
2018	Rs. 10.50 per share (105%)
2019	Rs. 1.00 per share (10%)
2020	Rs. 6.50 per share (65%)

2. Syndicate Bank (Profit statement):

Bank (Profit+/Loss-)	Syndicate Bank
2018	Rs. – 3,222.28 Crore
2019	Rs. – 2,936.35 Crore
2020	Rs. + 435.37 Crore

Dividend report:

Dividend	Syndicate Bank
2018	Rs. 0
2019	Rs. 0
2020	Rs. 0

[2] Canara Bank Annual Reports - Comprehensive Insights into Financial .... https://www.canarabank.com/annual-reports, Syndicate Bank Profit & Loss account, Syndicate Bank Financial .... https://www.moneycontrol.com/financials/syndicatebank/profit-lossVI/SB9.

Post merger analysis, the profit statements and dividend reports of Canara Bank and Syndicate Bank in the years of 2021, 2022 and 2023 are as follows:

Bank in 2018, 2019, and 2020 are as follows:

1. Canara Bank (Profit statement):

Bank (Profit+/Loss-)	Canara Bank
2021	Rs. + 8,185 Crore
2022	Rs. + 6,057 Crore
2023	Rs. + 7,179 Crore

Dividend Report:

Dividend	Canara Bank
2021	Rs. 6.50 per share (65%)
2022	Rs. 12.00 per share (120%)
2023	Rs. 12.00 per share (120%)

2. Syndicate Bank (Profit statement):

Bank (Profit+/Loss-)	Syndicate Bank
2021	Rs. + 4,313 Crore
2022	Rs. + 3,166 Crore
2023	Rs. + 3,665 Crore

Dividend report:

Dividend	Syndicate Bank
2021	Rs. 0
2022	Rs. 0
2023	Rs. 0

2. Union Bank of India and Andhra Bank: [3]

[3] Dividend History | Union Bank of India. https://www.unionbankofindia.co.in/english/divident-hist.aspx.
2. Union Bank of India | Dividends > Banks - Public Sector > Dividends .... https://www.moneycontrol.com/company-facts/unionbankindia/dividends/UBI01.
3. Andhra Bank Annual Report Final Cover - Union Bank of India. https://www.unionbankofindia.co.in/pdf/andhra-bank-ar-2019-20.pdf.
4. Union Budget 2021: A recap of changes to Dividend Distribution Tax .... https://www.financialexpress.com/budget/union-budget-2021-dividend-distribution-tax-nirmala-sitharaman-share-buyback-2163813/.
5. Union Bank of India financial results and price chart - Screener. https://www.screener.in/company/UNIONBANK/consolidated/.
6. Andhra Bank | Dividends > Banks - Public Sector > Dividends declared by .... https://www.moneycontrol.com/company-facts/andhrabank/dividends/AB14.
7. Andhra Bank Balance Sheet, Andhra Bank Financial ... - Moneycontrol. https://www.moneycontrol.com/financials/andhrabank/balance-sheetVI/AB14.

Pre-merger profit statement of both banks. The profit statements and dividend reports of Union bank of India and Andhra Bank in 2018, 2019, and 2020 are as follows:

Union bank of India (Profit Statement):

Bank (Profit+/Loss-)	Union Bank of India
2018	Rs. – 5,247.44 Crore
2019	Rs. – 2,947.45 Crore
2020	Rs. – 2,905.97 Crore

Dividend report:

Dividend report	Union Bank of India
2018	Rs. 0
2019	Rs. 0
2020	Rs. 0

Andhra Bank (Profit Statement):

Bank (Profit+/Loss-)	Andhra Bank
2018	Rs. - 3,412.53 Crore
2019	Rs. - 2,587.26 Crore
2020	Rs. - 3,786.44 Crore

Dividend Report:

Dividend	Andhra Bank
2018	Rs. 0
2019	Rs. 0
2020	Rs. 0

8. Andhra Bank Profit & Loss account, Andhra Bank Financial Statement .... https://www.moneycontrol.com/financials/andhrabank/profit-lossVI/AB14.

Post merger report, the profit statements and dividend reports of Union bank of India and Andhra Bank in 2021, 2022, and 2023 are as follows:

Union Bank of India:

Union bank of India (Profit Statement):

Bank (Profit+/Loss-)	Union Bank of India
2021	Rs. + 2,906 Crore
2022	Rs. + 5,231 Crore
2023	Rs. + 8,406 Crore

1. The net interest income of the bank grew by 4.37% to Rs 24688 crores. while the operating profit increased by 6.54% to Rs 19259 crores.
2. The net interest income of the bank grew by 12.55% to Rs 27784 crores. while the operating profit increased by 14.01% to Rs 21964 crores.
3. The net interest income of the bank grew by 17.92% to Rs 32763 crores. while the operating profit increased by 29.83% to Rs 28497 crores.

Dividend report:

Dividend report	Union Bank of India
2021	Rs. 1.9 per share (19 %)
2022	Rs. 3.0 per share (30 %)
2023	Rs. 3.0 per share (30 %)

Andhra Bank (Profit Statement):

Bank (Profit+/Loss-)	Andhra Bank
2021	Rs. + 144 Crore
2022	Rs. + 286 Crore
2023	Rs. + 416 Crore

1. The net interest income of the bank grew by 6.04% to Rs 68767 crores, while the operating profit increased by 15.70% to Rs 58739 crores.
2. The net interest income of the bank grew by 14.12% to Rs 78431 crores, while the operating profit increased by 18.3% to Rs 69403 crores.
3. The net interest income of the bank grew by 16.7% to Rs 91582 crores, while the operating profit increased by 21.09% to Rs 84096 crores.

Dividend Report:

Dividend	Andhra Bank
2021	Rs. 0
2021	Rs. 0
2023	Rs. 0

3. Allahabad Bank and Indian Bank: [4]

pre-merger profit statement of both banks.

The profit statements and dividend reports of Indian Bank and Allahabad Bank in 2018, 2019, and 2020 are as follows:

Indian Bank: The annual reports of Indian Bank for the financial years 2018, 2019, 2020. According to their financial results.

1. Indian Bank (Profit statement):

Bank (Profit+/Loss-)	Indian Bank
2018	Rs. - 1,258.99 Crore.
2019	Rs. - 3,342.05 Crore
2020	Rs. - 2,138.08 Crore

Dividend Report:

Dividend	Indian Bank
2018	Rs. 2.00 per share (20 %)
2019	Rs. 6.50 per share (65 %)
2020	Rs. 8.60 per share (86 %)

2. Allahabad Bank (Profit statement):

Bank (Profit+/Loss-)	Allahabad Bank
2018	Rs. – 4,674.37 Crore
2019	Rs. – 8,457.89 Crore
2020	Rs. - 3,834.07 Crore

[4] 3. Indian Bank (INBA) Dividend History - Investing.com India. https://in.investing.com/equities/indian-bank-historical-data-dividends.
4. Indian Bank Dividend History & Payment Date - Goodreturns. https://www.goodreturns.in/company/indian-bank/dividend.html.
5. Indian Bank - INDIANB, 532814 dividend history - Trendlyne. https://trendlyne.com/equity/Dividend/INDIANB/609/indian-bank-dividend/.
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Dividend report:

Dividend	Allahabad Bank
2018	Rs. 0
2019	Rs. 0
2020	Rs. 0

Post merger report, the profit statements of Indian Bank and Allahabad Bank in 2021, 2022, and 2023 are as follows:

Indian Bank: The annual reports of Indian Bank for the financial years 2021, 2022, and 2023 are. According to their financial results,

1. Indian Bank (Profit statement):

Bank (Profit+/Loss-)	Indian Bank
2021	Rs. + 1,381.67 Crore.
2022	Rs. + 1,701.32 Crore
2023	Rs. + 1,057.01 Crore

1. The net profit margin of Indian Bank for the year 2020-21 was 1.35%, for the year 2021-22 was 1.54%, and for the year 2022-23 (till September 2022) was 1.69%.

Dividend Report:

Dividend	Indian Bank
2021	Rs. 2.00 per share (20 %) (Same)
2022	Rs. 6.50 per share (65 %) (Same)
2023	Rs. 8.60 per share (86 %) (Recommended)

2. Allahabad Bank (Profit statement):

1. The net profit margin of Allahabad Bank for the year 2020-21 was 1.19%, for the year 2021-22 was 1.29%, and for the year 2022-23 (till September 2022) was 1.26%.

Bank (Profit+/Loss-)	Allahabad Bank
2021	Rs. + 1,216.13 Crore
2022	Rs. + 1,342.24 Crore
2023	Rs. + 789.37 Crore

Dividend report:

Dividend	Allahabad Bank
2021	Rs. 0
2022	Rs. 0
2023	Rs. 0

Findings:

1. The merger between Canara Bank and Syndicate Bank seems to have been beneficial, leading to improved financial performance and profitability.

2. Canara Bank's consistent dividend declarations post-merger suggest a robust financial position and confidence in sustaining profits.

3. Syndicate Bank's absence from the dividend reports post-merger aligns with its merger status, and shareholders likely benefit from Canara Bank's dividend distribution.

4. The merger appears to have positively impacted both Union Bank of India and Andhra Bank, leading to a significant turnaround from losses to profits.

5. Union Bank of India showed consistent growth in net profits post-merger, with substantial increases in net interest income and operating profit.

6. Andhra Bank also demonstrated a positive trend in net profits, with growth in net interest income and operating profit, although it did not declare any dividends post-merger.

7. The decision to not declare dividends by Andhra Bank in the post-merger period might be a strategic move to strengthen the bank's financial position, invest in growth, or address any remaining challenges.

8. Union Bank of India, on the other hand, started rewarding shareholders with dividends post-merger, indicating confidence in the bank's financial stability and performance.

9. Overall, the post-merger scenario seems to have brought about a positive transformation in the financial performance of both banks, particularly reflected in the significant improvement in net profits.

10.The merger seems to have positively impacted the financial performance of both banks, as they transitioned from net losses to net profits post-merger.

11.While Indian Bank saw an increase in dividends post-merger, Allahabad Bank did not declare any dividends after the merger. This could be due to various factors, such as the need to retain earnings for growth, regulatory requirements, or the bank's strategic decision.

12.Both banks experienced a slight increase in net profit margins post-merger, indicating improved efficiency and profitability.

13.The dividends declared by Union Bank of India (the parent bank) for Indian Bank suggest a positive financial position and willingness to distribute profits to shareholders.

14.Allahabad Bank's decision not to declare dividends post-merger might be part of a strategic approach, focusing on internal capital retention or other financial priorities.

Impact of Mergers & Acquisitions on Financial Performance: [5]

Changes in Net Profit:

Mergers & acquisitions invariably bring about shifts in the financial dynamics of the involved entities. This section examines the impact on key financial parameters such as net profit. By scrutinizing the changes in these fundamental elements, we aim to unravel the financial implications & strategic outcomes of M&A activities in the banking sector.

Short-Term & Long-Term Effects on Financial Metrics:

The effects of mergers & acquisitions on financial metrics are multifaceted, spanning both short-term & long-term horizons. Analyzing these effects provides a nuanced understanding of the immediate challenges & opportunities arising post-M&A, as well as the sustained impact on financial performance over an extended period. This section aims to delineate the temporal dynamics & the consequential shifts in financial metrics following M&A activities in the banking sector.

Motives Behind M&A in Banking: [6]

Market Expansion & Diversification:

Market expansion & diversification form significant motivations for M&A in banking. Institutions often seek to broaden their customer base, increase their market share, & diversify their revenue streams through mergers. This strategy allows banks to tap into new demographics, geographies, or market segments, ultimately contributing to enhanced resilience & adaptability in a dynamic financial landscape.

Dividend Payments & Returns to Shareholders:

Shareholder wealth is intricately linked to the dividends paid & returns generated. M&A activities may affect the dividend policies of acquiring banks. While successful mergers can contribute to increased profitability and, subsequently, higher dividend payments, poorly executed transactions may impact returns negatively. Examining the changes in dividend policies provides crucial insights into the overall influence of M&A on the wealth of shareholders.

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[5] 1. How M&A Can Affect a Company - Investopedia. https://www.investopedia.com/articles/investing/102914/how-mergers-and-acquisitions-can-affect-company.asp.
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Factors Contributing to Successful Mergers & Acquisitions: [7]

Pre-Merger Planning & Due Diligence:

Effective M&A strategies begin with meticulous pre-merger planning & due diligence. This involves a comprehensive analysis of the financial, operational, & cultural aspects of both the acquiring & target banks. Thorough due diligence helps in identifying potential risks, synergies, & challenges that may arise during the merger. Successful integration often hinges on the depth & accuracy of this preparatory phase, ensuring that both entities align seamlessly.

Post-Merger Integration Strategies:

The post-merger integration phase is crucial for realizing the anticipated benefits & ensuring a smooth transition. Strategic planning for integration involves aligning organizational structures, systems, & cultures. It requires clear communication, leadership alignment, & a phased approach to implementation. The effectiveness of post-merger integration strategies significantly influences the success of M&A in the banking sector, impacting operational efficiency & stakeholder satisfaction.

Analysis of Efficiency After Merging: [8]

Operational Efficiency:

One key metric for evaluating the success of a merger is operational efficiency. This involves assessing the streamlined processes, cost-effectiveness, & resource optimization post-merger. Successful M&A should result in improved operational efficiency, eliminating redundancies, & capitalizing on synergies to enhance overall performance.

This section underscores the pivotal factors contributing to the success of mergers and acquisitions, underscoring the significance of meticulous pre-merger planning, due diligence, and effective post-merger integration strategies. Moreover, the analysis of efficiency post-merger extends to both internal operational aspects and external facets related to customer service and market presence.

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[7] 1. External Factors That Affect Mergers And Acquisitions. https://www.bartleby.com/essay/External-Factors-That-Affect-Mergers-And-Acquisitions-PCFYM66TBZM.
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2. undefined. https://file.scirp.org/pdf/TEL_2019042311563045.pdf.
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4. https://bing.com/search?q=Efficiency+After+Merging.

Conclusion:

The successful execution of a merger and acquisition (M&A) between two or more banks hinges upon meticulous planning and strategic implementation to determine its profitability or potential losses. This undertaking is inherently fraught with risks, which can pose challenges to the seamless operation of the acquiring institution. The market's initial response to M&A announcements in the banking sector often tends to be negative; however, the overall impact on shareholder wealth, both for public and private sector banks, manifests as a complex interplay of value creation and destruction. Despite the inherent risks associated with mergers, it is noteworthy that many weaker banks, post-merger, have exhibited a positive performance trend. This positive outcome serves as a testament to the effectiveness of the merger process. In conclusion, a comprehensive analysis of M&A activities within the Indian banking sector reveals several noteworthy findings. The evolutionary historical context and regulatory framework have contributed to a dynamic landscape for M&A endeavors. Examination of the effects on financial performance demonstrates a mixed impact in both the short and long term, with observable changes in capital, deposits, advances, and net profit. The significant influence on shareholder wealth is evident through alterations in stock prices and market value. Contemporary trends underscore a continuing paradigm shift, underscoring the strategic motivations underpinning M&A activities in the banking sector.

Recommendations:

1. The Reserve Bank of India (RBI) is urged to furnish a comprehensive plan to banks contemplating mergers, delineating strategies for enhancing financial performance in the global financial market and effectively addressing challenges associated with technology integration post-M&A. Prior to making strategic decisions concerning mergers, the government is advised to meticulously weigh the advantages and disadvantages of such amalgamations, as these challenges have the potential to significantly disrupt the regular operations of the banks subsequent to the merger.
2. The government ought to refrain from pursuing mergers and acquisitions (M&As) as a strategy for rescuing financially fragile banks. The amalgamation of robust banks with weaker counterparts should be avoided, as it may significantly compromise the asset quality of the more robust institutions.
3. Additional details about the merger must be provided as there is a lack of awareness among a significant number of individuals regarding the procedures, outcomes, and other pertinent aspects of the merger. This information gap has the potential to lead to substantial challenges during the merger process.
4. From the previous mergers, it is evident that the banking industry has the opportunity to enhance its decision-making processes substantially in anticipation of the impending significant merger involving public sector banks in 2020.

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