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Merger and Acquisition of Commercial Banks in India

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ABSTRACT

The paper explores the Punjab National Bank, Oriental Bank of Commerce and United Bank of India to merge, Canara Bank and Syndicate Bank to amalgamate. Mergers aim to create fewer but stronger banks with larger balance sheets, better capital adequacy, and wider reach. The government announced the merger of 10 nationalized banks into four large lenders. Merger is a good idea. However, this should be carried out with right banks for the right reasons. Merger is also tricky given the huge challenges banks face. Mergers and acquisitions in the banking sector allow banks to increase economies of scale through consolidation. The framework will address mergers of state-owned banks, planned privatization in state-owned companies, minority stake sales, and the Centre's new exchange. Government of India decided to merge three Public Sector Banks namely – Bank of Baroda, Vijaya Bank and Dena bank into one single entity.

Keywords: merger, consolidation, nationalized, committee, financial, commercial, banking and sector

INTRODUCTION

Merger and acquisition (M & A) or consolidation as a critical tool of business strategy is now increasingly becoming popular not only in commodity producing corporate entities but also in financial service providers. From production industry to service sector including banking sector and software business, companies/banks are working overnight and are busy preparing their consolidation plans. Consolidation increases the market control and contact, diversifies the products and services thereby reducing the risk and redefines the competitive perimeter by acquiring different businesses. It also provides the bank with new capabilities, technologies and products, helps to over-come entry barriers and ensures direct entry into novel markets with lesser operating expenses.

The banking sector is the lifeline of any modern economy. It is one of the important financial pillars of the financial system, which plays a vital role in the successful/failure of an economy. Banks are one of the oldest financial intermediaries in the financial system. They play an important role in the mobilization of deposits and disbursement of credit to various sectors of the economy. The strength of economy of any country basically hinges on the strength and efficiency of the financial system, which, in turn depends on a sound and solvent banking system. In India, the banking sector is dominant as it accounts for more than half the assets of the In financial sector. “The bank descends from the Bank of Calcutta, founded in 1806 via the Imperial Bank of India, making it the oldest commercial bank in the Indian subcontinent. The Bank of Madras merged into the other two presidency banks in British India, the Bank of Calcutta and the Bank of Bombay, to form the Imperial Bank of India, which in turn became the State Bank of India on 1 July 1955” (Rajesh 2009: 8)

'Commercial Banks' in India are organized as joint stock companies and known as banking companies. These banks are primarily classified into Scheduled Banks and Non-Scheduled Banks. Scheduled Banks include nationalized banks, State Bank of India and its subsidiaries, Private sector banks, Regional Rural banks and foreign banks. “Indira Gandhi, the then Prime Minister of India, expressed the intention of the Government of India in the annual conference of the All India Congress Meeting in a paper entitled Stray thoughts on Bank Nationalization” (Austin, Granville 1999: 215)

Non-Scheduled Banks are those which are not included in the 2nd Schedule to RBI Act. “The next major government intervention in banking took place on 19 July 1969 when the Indira government nationalised an additional 14 major banks. The total deposits in the banks nationalised in 1969 amounted to 50 crores. This move increased the presence of nationalised banks in India, with 84% of the total branches coming under government control” (Banerjee, Abhijit 2024)

Commercial banks serve as the king pin of the financial system of India. They render many valuable services and functions. The primary functions of the commercial banks include-Acceptance of Deposits; Advancing of Loans; Investment functions; Credit Creation; Dealing in foreign exchange etc. and on the = other hand, the secondary functions of commercial banks include-Agency Services; General Utility Services; Merchant Banking; Factoring Services etc. Thus it is clear that Commercial Banks are serving as a link between savers and investors and so help in the credit-allocation process. In our country, Commercial Banks are described as factories of credit. It results in the economic progress of the country.

"Later on, in the year 1993, the government merged New Bank of India with Punjab National Bank." (Parmatam Parkash 2003: 360)

As a developing country, in India, small and big, strong and weak, rural and urban, public and private, banks coexist. The distribution of banks in terms of profitability is skewed. Some banks earn high returns but are operating inefficiently and some banks are competing fiercely for a small segment of the market. Private sector banks have already put in place the latest technology while some public sector banks are still struggling to maintain their capital adequacy and other requirements. Hence, there is a need to restructure the banking sector of India. Moreover, the winds of financial reforms have ushered in new changes and new competition which has forced banks to improve their competitiveness. Restructuring and consolidation is one of the major routes through which the Commercial Banks could bring in competitiveness. This restructuring strategy is also known as Mergers & Acquisitions (M & A), Joint Ventures, Spin Off, Dive-statures etc.

It is notable that the Indian banking sector is expected to open up fully from 2009 for the foreign banks. There is an urgent need for domestic banks to set their business right by consolidating their strengths and protecting their weakness before the arrival of another wave of com-petition.

Now a days, the Indian Banking Sector has entered in the second phase of reforms with restructuring of the banking set up by closing down the loss-making and non-viable branches, reducing the number of regional and zonal offices, revising the loan policy and procedure and downsizing of staff through voluntary retirement scheme. On the other hand, Retail Banking has become the principal growth driver for banks. Banks need to restructure themselves to offer retail banking products at competitive prices.

After the introduction of financial reforms, dramatic changes: After the introduction of financial reforms, dramatic changes have been observed in the structure business of banking Indian Narasimham Committee suggested that financially weak banks should be merged with financially strong banks. Consequently, failures or continued vulnerabilities and stress in any one commercial bank, however small in size, could well lead to unfavorable perceptions. The Committee recommended formation of 3-4 large banks with international presence, 8-10 banks with national presence, local banks with regional presence and presence of rural banks.

After the recommendations of Narasimham Committee, in the early nineties, New Bank of India merged with Punjab national Bank. It was a merger of a weak bank with a strong bank. In 1998, 20th Century Finance merged with Centurion Bank. In 1999, there were two mergers-Bareilly Corporation Bank merged with Bank of Baroda and Sikkim Bank merged with Union bank of India. In February 2000, Times Bank merged with HDFC Bank and in March 2001, Bank of Madurai merged with ICICI bank. ICICI Ltd. merged with ICICI bank on March 31, 2000, and converted itself into a Universal Bank. The Benares State Bank Limited was merged with Bank of Baroda on June 20, 2002. Three mergers were also made in year 2002 viz., Rajasthan Bank Financial Services Ltd. merged with The Bank of Rajasthan Ltd.; Andhra Bank Housing Finance Ltd. merged with Andhra Bank and Bank of India Finance Ltd. & BOI Asset Management Company Ltd. merged with Bank of India. All branches of Global Trust Bank were merged with Oriental Bank on August 14, 2004 and IDBI merged with IDBI Ltd. on January 1, 2005.

At present, SBI is in the process of consolidating operations of its various subsidiaries and associate banks. Under this process, 'State Bank of Saurashtra' has been merged with State Bank of India in Oct. 2007.

Recently, on December 16, 2008, the SBI has merged its Mauritius based subsidiary, 'Indian Ocean International Bank' (IOIB), with SBI International (Mauritius) to consolidate its operations in the African island nation. The new entity has begun operations as SBI (Mauritius). It is notable that IOIB has been operating in Mauritius since, 1978. The bank has 11 fully-integrated branches in major cities and towns, including Rodriguez, and has a network of 10 ATMs. SBI had acquired a majority stake in the bank in April 2005. SBI International, one of the first offshore banks to be established in Mauritius in 1990, began with a paid-up capital of $10 million. Its assets at the end of March, 2008 were $ 285 million as against $ 113.53 million a year ago. The new entity, SBI (Mauritius), began operations from October 25, 2008. On the domestic front, SBI plans to merge 'SBI Commercial and International Bank' [SBICI], its wholly-owned subsidiary, with itself and also take over SBISAP Securities to make it a direct subsidiary. The acquisition of SBICI has been approved by the boards of SBI and SBICI and it is necessary regulatory approval it is hoped that in near future, all remaining subsidiaries will also be merged with State Bank of India.

Although it is difficult to draw up a comprehensive list of factors propelling consolidation or M & A activity in Indian Banking Sector, yet the usual factors and motives behind bank mergers can be enumerated as under-

1. To achieve economies of scale and stable asset quality for smaller banks.

2. To acquire proper size through the less cumbersome inorganic route to meet competition.
3. To cut cost through branch and HR replacement and rationalizing.
4. To achieve geographical diversification and to diversify risk.
5. To acquire outstanding management or personnel.
6. To eliminate an acquirer's liability on account of tax benefit.
7. To increase the market share steadily.
8. To achieve better technological strengths for greater customer orientation and to have a wider array of low priced products for customers etc.

Though, there are definitely certain advantages emanating from synergy on consolidation of banks, there are also some disadvantages and problems/dangers from the Mergers and Acquisitions of banks viz. "In 2016, the board of SBI and the Union Cabinet cleared the proposal to merge the remaining five associate banks (State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala, and State Bank of Travancore) and SBI's fully owned subsidiary Bharatiya Mahila Bank with SBI" (Saha, Manojit 2016)

'The merger would see SBI entering the list of world's 50 largest banks by assets"(Iyer, Aparna 2016)
"Recent mergers (effective April 1, 2020)

- Indian Bank: Merged with Allahabad Bank.
- Punjab National Bank: Merged with Oriental Bank of Commerce and United Bank of India.
- Union Bank of India: Merged with Andhra Bank and Corporation Bank.
- Canara Bank: Merged with Syndicate Bank"(wikipedia)

"On 30 August 2019, Minister of Finance Nirmala Sitharaman announced the government's plan for further consolidation of public sector banks. The mergers took effect from 1 April 2020.
"The following banks were nationalized in 1980:

- Punjab and Sind Bank
- Vijaya Bank (now Bank of Baroda)
- Oriental Bank of Commerce (now Punjab National Bank)
- Corporation Bank (now Union Bank of India)
- Andhra Bank (now Union Bank of India)
- New Bank of India (now Punjab National Bank)" (wikipedia)

Allahabad Bank was merged into Indian Bank.
Oriental Bank of Commerce and United Bank of India were merged into Punjab National Bank.
Andhra Bank and Corporation Bank were merged into Union Bank of India.
Syndicate Bank was merged into Canara Bank." (Staff Writer 2019)
1. Regional flavors that the bank enjoys will be destroyed.
2. Objections of creditors of merging banks.
3. Judicial interpretations and elucidations.
4. Different customers engaged.
5. Always face different types of degrees of risk.
6. Service quality will suffer.
7. Fees and other charges will rise
8. Problem of low credit avail-ability for small and medium enterprise will worsen.
9. Human issues can create the following problems-
(i) Uncertainty and insecurity for the employees of the merging banks.
(ii) Fitting of the employees of the acquired banks into the acquirer bank.
iii) Human relation between the two banks' employees.
(iv) Difference in the service conditions.
(v) Matters relating to performance and competency levels.'
(vi) Difference in the Promotional & developmental policies.
(vii) Re-deployment of the employees in case of excess staff position etc.
10. Operational issues can create so many problems such as-
(i) Interest rates of deposits, loans & advances.
(ii) Asset quality or NPA levels.
iii) Difference in terms and conditions of products.
(iv) Variations in the services and facilities.
(v) Difference in the competency level of the employees.

(vi) Adjustment of culture of the employees in terms of their work culture, customs and practices and lifestyles.
(v) Different in the competency level of the employees.
(vi) Adjustment of culture of the employees in terms of their work culture, customs and practices and lifestyles.
(vii) Undisclosed items or off balance sheet items such as contingent liabilities can also generate problems etc.

CONCLUSION

These are really puzzling problems which need immediate remedial actions. Therefore, Indian Banks should learn the lessons from the above stated dangers/problems before embarking upon unbridled Mergers and Acquisitions. Consequences of subprime lending crisis, global financial turmoil & uproar and regulatory framework regarding to M & A activities should also be given due weightage while taking the decision of consolidation. The merger helps in financial inclusion and broadening the geographical reach of the banking operation. Thus will ensure inclusive and sustainable growth.

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