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A Study on the Amalgamation and Merger of Commercial Banks in India: Benefits, Consequences and Challenges

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DeepikaTiwari
Research Scholar,
Dept. of Commerce,
University of Lucknow,
Lucnow, Uttar Pradesh, India

Sunita Srivastava
Assistant Professor,
Dept. of Commerce,
University of Lucknow,
Lucnow, Uttar Pradesh, India

Abstract

The Economy of India is known for its endurance, from many years, it has faced a change continuously, global economic depressions, and many reforms of the government with ease. The banking sector of India has its own reputation and goodwill in the international level for maintaining and retaining its stability, even though the global economic environment and the emerging trends in financial sector pose challenges. The financial sector is considered as the lifeline and backbone of an economy. Many public sector banks in India; given this, acquisition and merger are a good idea in principle. The merger and acquisition of banks will definitely help the banks improve operational efficiency and customer services; this would involve synergies in the branch network, low-cost deposits and subsidiaries. But acquisition and merging of banks is not an easy task, because many public sector banks in distress and facing precarious and insecure situations. It is a challenging and difficult situation for the Government of an economy to identify stressed banks and motivate them to merge with a larger banks and an entity. In this research paper author has to examine the concept and reasons behind the consolidation and merger of Indian Banks, to recognize the banks, Non Profitable Assets (NPAs) during 2018 and 2019, appraise the benefits, implications, consequences and challenges of merger of Indian Banks, and to suggest the measures for achieving the goal of merger.

Keywords: Public Sector Banks, NPAs, Acquisition and Merger

Introduction

According to RBI, India's banking sector is adequately capitalized and well operated. The Financial and Economic conditions of the country are more remarkable than any other country in the world. The studies of Credit and liquidity risk suggest that banks of India are normally strong and have withstood the global decline well. Banking industry of India has recently noticed the roll out of new banking models. Among them the merger of weakness and loss incurring Public sector banks with the large banks is under significant debate. The merger and amalgamation are part of the government's efforts to strengthen the banking industry with an eye on apprehending the bad loan crisis. the Merger is an action taken by the government of India to help the rise in bad loans or NPAs at a time when corporate demand is weak. Mergers of banks are only the one way of managing the problem and difficulties and therefore cannot be totally discounted. However, the trick lies in ensuring that the merger fallout is managed judicially. The proposal is a part of a wider move to consolidate and amalgamate the banking system and reduce pressure on the national exchequer. RBI will observe Banks on their performance, especially in terms of NPA (Non-Performing Assets) and loans which are not recovered. If NPA (non performing assets) percentage of bank is above prescribed norms and limits, it will be asked to merge with a bigger bank to ease and alleviate the situation as the combined capital of Banks will be higher and thereby reducing the NPA (non performing assets) percentage. Currently there are 10 PSU banks under RBI's Prompt Corrective Action (PCA) framework. Like - Dena Bank, Allahabad Bank, United Bank of India, Corporation Bank, IDBI Bank, UCO Bank, Central Bank, Indian Overseas Bank, Oriental Bank of Commerce, Bank of Maharashtra and Bank of India with NPAs ranging from 15% to 31%.

Objective of the Study

The main objectives of the study are:

1. To understand the concept and reasons behind the consolidation and merger of Indian Banks.
2. To recognize the banks, Non Profitable Assets (NPAs) during 2018 and 2019
3. To appraise the benefits, implications, consequences and challenges of merger of Indian Banks.
4. And To suggest the measures for achieving the goal of the merger.

Research Methodology

The research paper on the title "A Study on the amalgamation and merger of commercial Banks in India: benefits, consequences and Challenges "on the basis of descriptive analysis study and method, which is based on secondary sources. For the purpose of this study, some articles and research papers on the relevant topics are studied.

Review of Literature

Jyoti H. Lahoti (2016): Proposed that merger and acquisitions are important corporate strategy actions that aid the firm in external growth and provide its competitive advantage. Mergers of banks are increasing in the current globalized economy, for improving competitiveness of companies through gaining greater market share, widening the portfolio to decrease business risk, entering new markets, geographies, and capitalizing on economies of scale.

Jayashree R Kotnal (2016): Mergers and Acquisition is a very important tool for the growth and expansion in any Industry and the Indian Banking Sector is no exception. It is very helpful for the survival of the weak banks by merging into the larger bank. This study shows the impact and result of Mergers and Acquisitions in the Indian Banking sector.

A.N.Tamragundi, Devarajappa S (2016): Examined and analyzed the effect of mergers on the performance of some selected commercial banks in India. The effect of mergers on the financial performance of the banks has been assessed from three prospective. There is a notable improvement in Deposits, Advances, Businesses and Number of Employees of all selected banks. This result indicates that Mergers can help commercial banks achieve and accomplish physical performance.

Gurbaksh Singh, Sunil Gupta (2015): Compared and differentiate pre -and - post mergers performance of the selected banks after the 1990 and collected the data and information. The effect of mergers, changes in profitability which is returned on Capital Employed, Return on Net Worth, Operating Profit Margin and other financial ratio is compared. The financial performance of the banks has grown which margin to the gain of selected public and private sector bank in Indian Banking Sector.

To Understand the Concept and Reasons behind the Acquisition and Merger of Indian Banks

The very first consolidation and merger of the bank was recommended in 1991 by the committee of Narsimhan under the chairmanship of Maidavolu Narsimhan (former Governor, Reserve Bank of India, RBI). The Committee endorsed that the actual numbers of commercial banks need to be decreased in number. For this purpose they suggested a 3-tier banking structure. In 1998, the committee rethinking the suggestions for merger and consolidation of large Indian banks to make them strong enough for supporting international trade import and export. Its recommendations and suggestions are –

1. There should be 3 to 4 large commercial banks, which be developed as international banks at the top.
2. These commercial banks will have an international presence.
3. Then there should be 8 to 10 banks having a nationwide presence should focus on the national and Universal banking financial services.
4. Local banks focus on region-specific banking services.

The financial year 2016–17, was one of the challenging and tough year for all commercial banks (PSUs), with their whole net loss of Rs.11,865 crore. This financial year was the year when the gross and net non-performing loans (NPAs) of banks were at a peak. The government is now very serious for deliberation of reducing the number of Public sector banks (PSUs) from 21 to 12 with an aim of creating 3 to 4 large global sized banks. This decision and their implementation will add to the operational strength of the PSU (public sector banks) banks. The Main aim and objective of RBI (reserve bank of India) in bank merger is merging weak banks in the terms of high NPAs merge with strong banks to prevent loss to depositors and making banking sector strong which is automatically strong the condition of our economy too. This is done only on the basis of the evaluation found in the examination report conducted; section 35 of the Banking Regulation Act, 1949.The merger and acquisition of commercial banks is under the policy of central government. According to Financial services secretary Rajiv Kumar, he suggested two guiding principle for the merger is –

1. To create or develop a financially healthy bank that was larger in size.
2. To have an institution that had a strong brand , good reach and technology

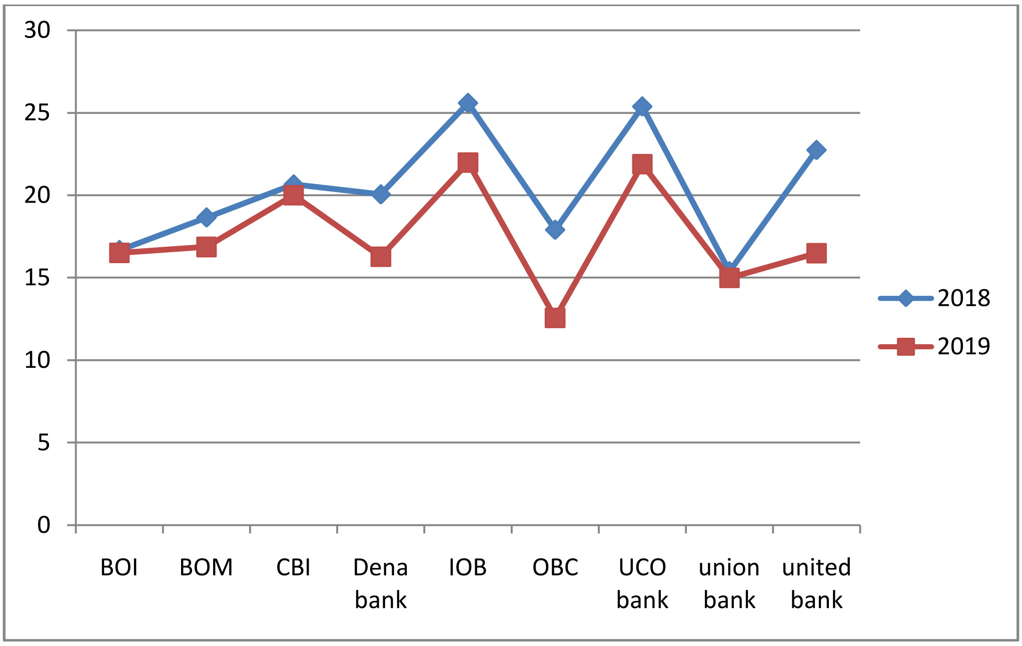
To recognise the banks Non Profitable Assets (NPAs) during 2018 and 2019

Table No. 01

Public Sector Banks; comparision of NPAs

S. No.	Banks	Gross NPA % 2018	Gross NPA% 2019
1	Bank of India	16.66	16.50
2	Bank of Maharashtra	18.64	16.86
3	Central bank of india	20.64	19.99
4	Dena bank	20.04	16.27
5	Indian overseas bank	25.58	21.97
6	Oriental bank of commerce	17.89	12.56
7	UCO bank	25.37	21.87
8	Union bank of India	15.73	14.98
9	United bank of India	22.73	16.48

Source: RBI, Ace Equity, Government announcements and Source: http://www.economictimes.com



Source: RBI, Ace Equity, Government announcements and Source: http://www.economictimes.com

In 2019 non-performing assets (NPAs) are decreasing as compared to 2018 NPAs just because of the merger of some banks. India faced many financial problems during the period 2016, 2017 and 2018 but the action of merger of banks decision taken by RBI is slowly slowly improving the situation of our country.

Latest Merger and acquisition of (Bank of Baroda, Vijaya Bank and Dena Bank)

The recent one is the trio of Bank of Baroda, Vijaya Bank and Dena Bank. BOB take over Dena bank and Vijaya Bank. The government recommended the merger of these 3 banks aimed at making the country's 3rd -biggest lender. Bank of Baroda is the biggest among the three with Rs 10.29 lakh crore of total business, followed by Vijaya Bank and Dena Bank. In this consolidation, the government found the right fit. "Dena Bank has a strong Current Account and Saving Account (CASA) base with a good retail and the presence of small scale industry (MSME). Vijaya Bank was pragmatic in its lending and providing, Bank of Baroda offers a congenial international presence, a strong brand and a very good technology platform will result and conclusion in a large cost rationalization and deliberation.

Table No. 02

Overall Financial Standing of The Three Banks and Their Combined Entity

S. No.	Parameters	Punjab National Bank	Union Bank	Oriental Bank Of Commerce	Merged Entity
1	Total business (in lakh crs.)	10.28	2.78	1.7	14.76
2	Total deposits (in lakh crs.)	5.80	1.57	1.03	8.4
3	Gross advances (in lakh crs.)	4.48	1.22	.64	6.34
4	Net NPAs	5.4	4.1	11	20.5
5	CRAR %	12.13	13.91	10.6	12.25
6	Branches	5,502	2,129	1,858	9490
7	employees	56,361	15,874	13440	85,675
8	Net profit/loss (in crs.)	528 cr. profit	144 cr profit	-721 cr loss	

Source: http://www.economictimes.com

The finance ministry stated that the provision coverage ratio (PCR) of the proposed amalgamated entity will be 67.5%, well above the average of public sector banks (PSBs) at 63.7%. The capital adequacy ratio of the combined entity would be at 12.25%, significantly above the regulatory norm of 10.875%. One of the reasons for choosing these 3 banks was that the two stronger ones will absorb the weaker entity.

Other major mergers

1. Punjab national bank take over oriental bank of commerce and united bank of India 1 April 2020
2. Canara bank take over syndicate bank 2020
3. Bank of baroda take over dena bank and vijaya bank april 2019
4. Life Insurance Corporation of India taking over IDBI Bank (2018)
5. ING Vysya Bank merger with Kotak Mahindra Bank In Nov 2014
6. The Bank of Rajasthan merger with ICICI Bank in 2010.
7. Centurion Bank of Punjab merged with HDFC Bank in 2008
8. The Sangli Bank merger with ICICI Bank in 2007.
9. Bharat Overseas Bank merger with Indian Overseas Bank (IOB) in 2007.

10. Global Trust Bank merger with Oriental Bank of Commerce (OBC) in 2004
11. South Gujarat Local Area Bank Ltd merger with Bank of Baroda in 2004.
12. Benares State Bank Ltd merger with Bank of Baroda in 2002.
13. Times Bank Ltd. merged with HDFC Bank in 2000.
14. New Bank of India merger with Punjab National Bank (PNB) in 1993.

Benefits of Bank Merger

"This is a progressive move and signifies the government's determination to strengthen the banking sector in the country for a better performance and service delivery,"

– Rashesh Shah, former President of FICCI

1. Cost of banking operation reduces: Merging and consolidate with larger bank will definitely help to increase banks' margins by lowering the deposit rates. A big entity can easily manage its short and long term liquidity better. There will be low requirement for overnight borrowings in call money market and from RBI under Liquidity Adjustment Facility and Marginal Standing Facility.
2. Expanding the geographical reach: The geographical reach of banking services can be easily achieved by the merger of large public sector banks. The advantage of their expertise the merger and acquisition will help the most geographically concentrated regionally present banks to expand their coverage.
3. Good Risk management and fall in NPAs: larger capital base and higher liquidity, the pressure on the central government to recapitalize the public sector banks will come down substantially. Large banks would have a larger capital base enabling them to offer big ticket loans on their own without being part of a company.
4. Access to a larger customer base: A bank merger helps a bank to scale up quickly and gain a large number of new customers instantly. The Customer will now have a number of branch accounts and ATMs to access their accounts. Another advantage for the customers is the charges on cross bank ATMs usage would decrease considerably.

Fill up Technology Gaps

Bank mergers and acquisitions will help the banks to fill product or technology gaps. From a technology point of view, the acquisition of a small bank by a larger bank might allow the smaller bank to upgrade its technology platform significantly.

Better control of RBI

Better control of the system and implementation of policies will be seen from RBI. Since, it is comfortable for RBI to regulate few banks from regulatory Perspective; monitoring and control of less number of banks will be easier.

Lowering Scale of Inefficiency

The large scale, expertise available in many of the sphere of banking operation, the scale of inefficiency which is occuring more in case of smaller banks, will be minimized. The system could be better, if the banks are consolidated into fewer but healthier banks.

Consolidated growth of the Banking Sector

Larger size of the Bank will help the merged and consolidate banks to offer more products and services. Smaller banks in size have repeatedly and again, again failed to maintain their asset quality. If the small banks merge, integrated and consolidated into larger ones which have the capability to do an appraisal of projects and large businesses they can grow with less risk.

Better Use and Management of Human Resources

The human capital and resource in the banks will be better managed, better unification of the workforce, centralized transfer system, uniformity in pay-scales, and consistency in terms of employment policy. Acquisition and merger will also increase capital efficiency, apart from improving the ability of banks to recover bad loans which are rising.

Greater Remembrance of Indian Banking

In the global market, the Indian banks will gain greater identification and higher rating. The acquisition and merger will help create a strong international competitive bank with economies of scale and enable the realization of wide ranging synergies.

Acquisition and Merger of Infrastructure

With a centralized system, non-productive competition is wiped out, a centralized management system will save the time wasted in the transaction, paperwork and delegation are reduced. This has a snowballing effect where the system is able to function as a well oiled system, with minimal hindrances and difficulties in day to day functioning.

Financial Savings

Multiple posts of CMD, CEOs, General Manager and Zonal Managers (ZM) will be reduced, resulting in substantial financial savings. All Bank staff will be coming under a single umbrella in regard to their service conditions and wages instead of facing disparities.

Major Challenges

1. V.A. Joseph, the Managing Director, Federal Bank suggests that "most accession to India was born out of compulsions and over 90 per cent of past accession had failed to accomplish the objectives".
2. Many banks pay attention on regional banking requirements. With the merger and consolidation the very purpose of establishing the bank to cater the regional needs is lost. The Large international banks had disintegrated during the global financial crisis and recession, such as Deutsche Bank, while smaller ones had survived the crisis due to their strengths and focus on small aspects.
3. The weaknesses of smaller banks are transferred to the big bank by merging them. It will be very difficult for the all the banking system to survive. The SBI, which merged and integrated five of its associates and Bharatiya Mahila Bank with itself, last year, has been struggling with losses for the last three successive quarters (Q1FY19 loss was Rs 4,875 crore).

4. Forced mergers and acquisition make little business sense for the stronger banks as they are unlikely to solve the bad loan crisis that has grasped the banking system as a whole. It is important to ensure that such mergers and acquisition do not end up creating an entity that is weaker than the original pre-merger strong bank.
5. Technology integration in theory is easy to accomplish, but in practice it will desire a lot of hard work like just getting a new account code for all customers and communicating that will not be a very simple thing. Replacement of cheque books, RTGS, NEFT details and net banking interface will create confusion among consumers.
6. Major concern was the possibility of reduction and decrement in the employment, which has erupted opposition from the employees/Unions about the possible fallout of such merger and the effect of these on their job security, service conditions and career progressions and succession in their respective banks.

Consequences

1. The government contemplates that there will not be a reduction in workforce; however, there are probability that future recruitment will be having lesser vacancies since the bigger organization is already having the adequate work force. On account of merger and acquisition employment situation may disintegrate.
2. Employees of smaller banks lose recognition of their organizations and they will have to increase their efficiency to match with the equivalent in parent units. Thus, Integration of people will be a major challenge in merger and acquisition.
3. Customers who are assigned new account numbers or IFSC (Indian financial system codes) will have to update these details with various third-party entities: Income tax department for tax refunds, insurers to get maturity rewards, mutual funds to get the retrieval amounts and the National Pension System (NPS).
4. Customers will have to deal with the branch justification exercise. The current IFSC and MICR code applicable to the branch and account will be replaced, funds transfer and other financial transactions will also slow down.
5. The number of public sector banks will decrease, perhaps to 6 or 7, after the proposed acquisition and merger of banks. This will end the non-healthy and intense competition going on even among public sector banks as of now. Customers will have less choice of banking.
6. Financial inclusion plans may be pretentious and the deadline for their execution may be delayed. 'Direct Benefit Transfer' (DBT) of government aid, subsidies, grants also will be affected.
7. Leads to closure of bank branches in different parts. Discord and confusion among the consumers is common. The consumer can feel a sense of loss of their bank and its friendly employees. Further, consumers will have less choice of selecting a bank.

Suggestions

1. The central government shall not in hurry towards the process of bank merger. Because, it requires and wants a careful study of the financial status of banks in depth, detail and sufficient time to implement the scheme of mergers.
2. The decision with regard to selection of anguish banks for mergers with larger and stronger banks is to be taken carefully and grouping of various banks for this purpose is the key issue.
3. The acquiring bank shall not attempt to control or influence or subsume the acquired bank. The good aspects of both the banks before merger should be combined, in order to build confidence in all stakeholders, shareholders and to produce better results.
4. Employees will have to undergo sporadic or irregular training programs to get acquainted with the philosophies, processes and technology in the new environment.
5. The management must be ready with a good roadmap for this and allot substantial budgetary resources for this purpose.
6. There shall be conscious and organized, managed efforts to synthesize the differing organizational cultures, for the mergers yield the desired results.

Conclusion

Amalgamation and Merging of two financial institutions is unmanageable and not a very easy task in terms of integrating the accounts, infrastructure, management and marketing policies and many more of merging banks. It will take a lot of persistence to complete the merging process. After analyzing the above facts, though this is better idea of good governance, but the consolidation and merger of banks cannot be successful until and unless issues of corporate governance, structural issues related to them are resolved. The current merger of banks, the Bank of Baroda has taken over Dena bank and vijaya bank is seen as a rescue mission for Dena Bank. The outcomes have to be seen in the near future. The recent merger of Punjab national bank, Canara bank and united bank of India face some problems and difficulties, but the move of consolidation and merger of banks maybe there will be some difficulties, but this will give the long-term benefits and boost up the financial position of an economy.

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