

MERGER OF BANKS: NEED OF THE HOUR

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ABSTRACT

The banking sector holds a significant position in all economies and is one of the most fast growing sectors in India. Competition is tough. Regardless of the challenge of multinational players, national banks, both public and private, are tough in their quest for a competitive advantage by acquiring or merging potential opportunities like those offered today. As a result, mergers and acquisitions in financial sectors are a matter of the day. Commercial banks in India are undergoing drastic changes in the regulatory environment, phenomenal growth in off-balance sheet financial management tools, the introduction of e-commerce and internet banking and a significant consolidation of the financial industry. All these forces made the Indian banking sector very competitive. In this context, studying the performance of banks after integration becomes important.

KEYWORDS: Mergers, Govt. Sector, Private Sector; CAGR, Employee Productivity, e-Commerce.

Introduction

The various committees appointed by the Government of India have called for unification. They recommended that we need to have three or four major nationalized banks to improve operational efficiency. The Second Committee specifically stressed the need for Indian banks to be comparable in size to the world's leading banks. Narsimhan Committee proposed a three-tier banking structure in India with about 3-4 mighty banks to take up the position at the global level, 8-10 banks to be provide national coverage and the remainder to cover local coverage.

Most mergers have been forced into the pre-reform period. The post-reform era saw both forced and voluntary mergers. Enforced mergers resulted from the poor financial health of the banks that were acquired. Banks that experienced a decline in net worth, huge national programs of action and a decline in capital adequacy required the regulatory authority to undergo a merger. The acquisition by the World Bank's Eastern Commercial Bank Trust is a live example of forced integration. The main objectives of voluntary mergers are expansion, diversification and growth. The acquisition of Times Bank from HDFC and the acquisition of ICICI by Madura Bank are some examples of voluntary mergers. India has also seen cross-border acquisitions recently. The acquisition by SBI of a bank in Mauritius is an example of such a case.

Literature Review

Azeem Ahmed Khan (2011) explored various motivations of Merger and Acquisitions in the Indian banking sector. He concluded that the banks have been positively affected by the Merger and acquisitions. These results also suggested that merged banks could attain efficiency and profits through Merger and Acquisitions and could pass the benefits to the equity share holders as dividend.

Devarajappa S, (2012) explored various motives of merger in Indian banking industry. He also compared pre and post merger financial performances of merged banks with the help of financial standards like, Operating Profit Margin, Gross Profit margin, Net Profit margin, Return on Equity, Return on Capital Employed, Debt Equity Ratio etc. In totality the study indicates that the mergers have positive effect on banks.

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Need for Consolidation of Banks

- Economies of Scale: Assocham Survey has found that size of Indian banks in terms of their assets stands very small to make optimal use of their capacities to raise funds at internationally competitive rates. Combined assets of top ten banks counts for less than 60 per cent of GDP unlike the banking system of European economies, where even after the global financial crises, assets of only top five banks has grown to four times of GDP.
- Indian Banks are Too Small: Even as India is the second largest growing market for banking services after China in terms of the number of wealthy households, the ASSOCHAM Chief said, only two Indian banks, State Bank of India at the 64th position and ICICI Bank Ltd. at 81st, figure among the global top 100 by tier I capital – a core measure of a bank's financial strength that consists largely of shareholders' capital.
- Similarly, in terms of assets, India's largest bank, SBI is now the world's 70th largest bank. On the other side, ICICI Bank Ltd, the largest private sector bank has achieved the 148th position. No other Indian banks stand among the top 200 banks in the world-in terms of assets.
- Many specialists in Banking field finds that the fragmented nature of the banking industry, Indian banks are unable to compete at international level in terms of fund mobilisation, disbursal of credit, investment and rendering financial services. The balance sheets of top most Indian banks reveal that there is greater scope of consolidation to have the benefits of large sized globally competitive Indian commercial banks.
- Merger will Increase Capital Efficiency: Consolidation will also increase capital efficiency. Merged banks will have more options to raise capital.
- Would Decrease NPA: At a time when NPAs are mounting up, and banks are putting all kind of effort in recovery, the ability to recover through small number of banks will be higher while individual bank's exposure may go up. It is so as there are small numbers of mind whereas in the joint lenders' forum there are many minds and each bank has a different right with its borrower and that's why they often not agree on a common recovery plan. With consolidation the recovery will be more focused. Thus consolidation could decrease NPA in India.

Benefits of Bank Merger

- The merger will reduce the cost of the banking process.
- The motive of financial inclusion and geographical expansion of the Bank can be attained better by merging large banks into the public sector and benefiting from their experience.
- Consolidation will lead to better risk management and NPA
- With extensive experience in all areas of banking operations, greater inefficiencies will be reduced in the case of small banks.
- The merger will help geographically focused regional banks to expand their coverage.
- The size of the large bank will help emerging banks provide more policies and services and will contribute to the overall growth of the banking sector.
- Integration will help to improve professional standards.
- The largest SBI can manage liquidity better in the short and long term. There will be no need for overnight loans in the money market and RBI under the Liquidity Adjustment Facility (LAF) and the Terminal Marginal Facility (MSF).
- In the global market, Indian banks will receive more appreciation and high qualifications.
- With a larger capital base and greater liquidity, the central government's burden on recapitalizing public-sector banks over and over again will decrease significantly.
- Multiple positions will be eliminated for managers of CMD, ED, GM and Zonal, which will achieve significant financial savings.
- The staff of the Bank will be under one umbrella with respect to their terms of service and salaries instead of facing disparities.

Side Effects

- Many banks focus on regional banking requirements. With the merger the main purpose of establishment of the bank to serve to regional needs is lost.

- Large bank size may create more problems. Several large global banks collapsed due to the global financial crisis while smaller ones had survived the crisis due to their strengths and objective of serving micro aspects.
- Along with the mergers, the problems of the small banks also get transferred to the larger bank.
- As so far minor losses and recapitalization could regenerate the capital base of small banks. Now if the banking giant SBI depicts huge loss on account of high NPAs, as it had been incurring, it will be difficult task for the entire banking system to sustain.

Key Challenges

- It is useful to remember that in a growing and dynamic economy, there is the possibility of managing an efficient and profitable bank without looking to be a high-priced lender or creating a large balance sheet under global scrutiny. An independent assessment of the scope of mergers in the PSB should analyze whether there are alternatives to be considered for the long-term safety of "weak" power distribution centers, which can also reduce the pressure for additional capital.
- For integration or any other restructuring option, PSBs face the main challenge of severe talent shortages and the absence of adequate people in sufficient quantities. Almost all PSB devices in fusion radar lack the talented staff to effectively manage even existing processes.
- Many case studies have shown that merger ads generate confusion, anxiety and insecurity in employees, leading to a slowdown in business. Managing bad talent and poor communication often exacerbates these challenges. PSBs need leaders with vision, maturity, strong operational knowledge, persuasive skills and the ability to advance a diverse team to implement an effective plan.
- The short stay of senior PSB leaders prevents the launch of any strategic initiative. Proposals on how to bring the appropriate talent to the PSBs have remained at various levels and ensure staffs stay for a longer on paper.
- Therefore, the immediate task must be to promote talent in institutions "anchors" before starting mergers. It should be noted that hiring suitable people in the market and attracting experienced executives from other banks by offering better payment packages deserves to be considered among other things.
- Talent leadership must be able to work on integrating the cultures of two compact banks. Culture remains a dominant barrier to effective integration throughout the world. Despite the clear uniform culture in the PSB, there are wide variations of the regional background and several intangible factors. Although private banks have tried to formulate a unified culture by taking some stringent measures, such as imposing segregation of employees (which was adopted by ICICI to the Banco de Madura team after its merger in 2001), this is rare in PSB .
- Integration of human resources in matters such as compensation, publication and performance evaluation may be tough for the PSB. While this was quite improper in the merger of the National Central Bank with the new bank in India, it is known that the IDBI Bank has recently gone through several problems in trying to rationalize the human resources policies of the former development bank employees with the flow of commercial banking services.
- The other major challenge is in front of technology. Unlike the merger of the SBI, there is no similarity in PSB's IT architecture, with each bank employing multiple suppliers to develop their system. Banks are currently in various stages of implementing new initiatives with existing or additional suppliers. Formulating uniformity and applying a common system that fully covers all aspects of banking in the merged entity will be a challenge that can be extended for a long time.

Future Approach

First, it would be wise to start with two PSB centers installed, each preparing to take over one PSB, preferably small. The goal should be to complete integration within 12 months for example and create a template for future mergers. The consideration of previous mergers of the Reserve Bank of Indonesia was to enable the acquired bank to expand its presence in areas where there is no adequate presence. Therefore, at the request of OBC acquisition of GTB, it was said that the network of branch offices in the south region, where OBC lacks its presence, can help it become a larger national bank.

Such considerations have no relevancy with the advent of alternatives to banks and mortars. It would make sense to marry banks that have announced common identities that can help promote cultural achievement and rationalize the network. There should be guidance that after integration, the branches must be rationalized to eliminate overlaps within a clear time frame. Second, before the merger, non-bank investments should be evaluated for program distribution projects identified in areas such as insurance, brokerage and investment banking in a monetary manner, in order to require banks to exit or spend the investment within a fixed time frame that may be necessary to focus on banking rather than scattering rare talent to look for irrelevant areas.

Thirdly, it is important to consider whether one or more PSBs can be "weak" to play a regional role, or in a particular part, rather than continue to exist throughout India, or as multifunctional entities. The private sector already has good opportunities for small banks or small and medium-sized enterprises (SMEs), trade, finance and agriculture. There is solid logic for some PSBs to assign exclusive roles in these parts. India needs to maintain an appropriate balance between public and private sector ownership in banking for some time. Even with 150 national commercial banks and a large number of cooperative banks, only about 40 per cent of adults have formal bank accounts, and there are severe problems of poverty and regional disparities that can be dealt with. We need a mix of efficiently managed PSBs and powerful private banks to meet both development and social equity goals.

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