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Mergers and Acquisitions in the Banking Industry: An Evaluation

The only way to manage competitiveness is cost reduction through acquisition, which enables the bankers to spread its overhead cost over a large customer base. From the current trends, one can safely predict that consolidation will also be one of the effective strategies widely adopted by the bankers. This study attempts to assess the successfulness of Mergers and Acquisitions strategy in banking industry. It analyses the implications of takeovers from the financial point of view.

Dr. M. Selvam, * S. Vanitha* and M. Babu *

The banking industry is an important area in which mergers and acquisitions do make enormous financial gains. The traditional corporate customers of a banker turn away increasingly from traditional loan. They are in favour of alternative sources of financial instruments like commercial papers etc., As a result of changes in the expectation of the corporate customers, banks are now constrained to rethink their business and devise new strategies. On the other hand, competitors both from India and abroad are encroaching upon every area of business in the prevailing policy of LPG. Therefore, Indian bankers have to struggle to survive in a competitive environment. In the changed environment, bankers adopt different strategies. They have no other option except to reduce their costs (both operational costs and the cost of credit) The only way to manage competitiveness is cost reduction through acquisition, which enables the bankers to spread its overhead cost over a large customer base. From the current trends, one can safely predict that consolidation will also be one of the effective strategies widely adopted by the bankers.

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Statement of the Problem

It is common knowledge that dramatic events like mergers, takeovers and restructuring of corporate sectors occupy the pages of business newspapers almost daily. Further they have become the focus of public and corporate policy issues. This is an area of potential good and harm in corporate strategy including banking industry. Hence the proposed evaluations study on Mergers and Acquisitions. This study attempts to assess the successfulness of Mergers and Acquisitions strategy in banking industry. It analyses the implications of takeovers from the financial point of view.

Objectives or the Study

The main objective of this study is to analyse and compare the financial performance of merged banks before and after merger.

Methodology or the Study

The study is intended to examine the performance of merged banks in terms of its growth of total assets, profits, revenue, investment and deposits. The performance of merged banks is compared taking four years of pre-merger and four years of post-merger as the time frame. The year of merger uniformly included in the post- merger period of all sample banks. A random sample of seven banking units (The list is given in Table-I) was drawn from the list of 20 banking units, which have undergone mergers and acquisitions (The list of merged banks in India is given in Table-II). A sample of 35% of merged banks (7) from total merged bank. (20) was drawn. While drawing the sample banks for this study. the availability of financial data such as financial statement. history of the companies etc. was taken into account.

Data Collection of the Study

The present study mainly depends on the secondary data. The secondary data were collected for four years before and four years after the merger. The required data were obtained from the Prowess Corporate Database Software of CMIE. Chennai.

Tools used for Analysis

As stated earlier, this study has analysed the growth of total assets, profits, revenue, investment and deposits of merged banks before and after the merger. In order to evaluate the performance. the statistical tools like mean standard deviation and t-test have been used. The growth rates of sample banks for all variables (mean values of variable before and after merger) have been analyzed.

Analysis of the Study

For the purpose of this study analysis was made in terms of the following variables: (basic motives for undertaking merger & acquisition)

(a) Changes in Growth of Total Assets of Merged Banks,

(b) Changes in Growth of Profits of Merged Banks,

(c) Changes in Growth of Revenue of Merged Banks.

(d) Changes in Growth of Investment of Merged Banks

(e) Changes in Growth of Deposits of Merged Banks.

a. Changes in Growth of Total Assets of Merged Banks

Assets represent economic resources that are the valuable possessions owned by a firm. Assets are mainly used to generate earnings. The total assets refer to net fixed assets and current assets. The growth of total assets indicates firm's ability to produce large volume of sales and to earn larger revenue. One aim of business strategy namely, merger and acquisition is the maximization of total assets of merged banks i.e., firms' ability to produce large volume of sales. It is expected that the bank units after merger would function efficiently.

Table-3 shows changes in average total assets and its variability of sample merged banks. It is clear that all sample-merged banks (State Bank of India, Oriental Bank of Commerce, Centurion Bank of India, Bank of Baroda, Union Bank of India, HDFC Bank and ICICI Bank) have shown a tremendous upward growth in total assets after merger. The result of standard deviation clearly shows that the variation of assets of all merged banks after merger was high than that of pre merger period. As stated earlier, the t- test was used to test the significance of average change in total assets of merged bank after merger. The application of t-test revealed that all merged banks (State Bank of India, Oriental Bank of Commerce, Centurion Bank, Bank of Baroda, Union Bank of India, HDFC Bank and ICICI Bank) got significant 't' values in their assets growth. The analysis of growth rate (mean value) of total assets of sample banks clearly showed that ICICI Bank achieved high rate of growth (1387.03), followed by Centurion Bank (761.24), HDFC Bank (717.49), Oriental Bank of Commerce (136.16), Union Bank of India (74.50), Bank of Baroda (64.70) and State Bank of India (57.62).

b. Changes in Growth of Profits of Merged Banks

The profit is an indication of the efficiency with which the business operations are carried out by corporate sector. The poor operational performance may result in poor sales leading to poor profits. The merger intends to boost profits through elimination of overlapping activities and to ensure savings through economies of scale. The amount of profit may be increased through reduction in overheads, optimum utilization of facilities, raising funds at lower cost and expansion of business. The merged banks are expected to grow fast in all aspects and the expectations of stakeholders of both acquiring and merged banks could be fulfilled. Here the profit refers to profit before tax.

Table-4 illustrates changes in average profit and its variability in select merged banks. According to the Table, the average profit earned by merged banks taken for this study during post-merger period was higher than the profit earned during pre merger period. The standard deviation has shown that the variation in the growth of profits during post merged period was higher than that of pre merged period in the case of State Bank of India, Centurion Bank, Union Bank of India, HDFC Bank and ICICI Bank. In the case of other two banks (Oriental Bank of Commerce and Bank of Baroda) the variation during pre merged period was higher than that of post merged period. The 't' test clearly showed that the Centurion Bank, Bank of Baroda, HDFC Bank, ICICI Bank, State Bank of India and Oriental Bank of Commerce have significant profits earned by them. This shows that growth of profits of all merged banks except Union Bank of India - is statistically significant while the growth of profits of Union Bank of India is insignificant. It is understood from the growth rate (mean value) that ICICI Bank achieved highest growth rate in respect of profits among sample banks. The low growth rate was seen in Union Bank of India.

c. Changes in Growth of Revenue of Merged Banks

The revenue is earned from the main line of business. Generally, it excludes like income - non-recurring income and extraordinary income. The economic activity of a company is considered to classify the income. In the case of financial institutions including banking units, interest income is treated as main income. For the purpose of this study, revenue income refers to interest received, dividend earned, security transactions, leasing and hire services, bill discounting, exchange transactions, commission and brokerage and others.

Table-5 presents change in average growth of revenue income and its variability of sample merged banks. It is clear that the merged banks like State Bank of India, Oriental Bank of Commerce, Centurion Bank, Bank of Baroda and Union Bank of India, HDFC Bank and

ICICI Bank have shown a tremendous growth in revenue income after merger rather than the revenue income of merged banks before merger. The result of standard deviation indicated that there is more variation in the growth of revenue of all merged banks during post merged period than that of pre merged period. The t-test brought out the fact that all merged banks like State Bank of India, HDFC Bank, ICICI Bank Oriental Bank of Commerce, Centurion Bank, Bank of Baroda and Union Bank of India have achieved significant growth of revenue. The mean growth rate regarding revenue income clearly indicates the fact that the ICICI Bank achieved high growth rate following by Centurion Bank (1029.38), HDFC Bank (533.27), Oriental Bank of Commerce (140.32), Union Bank of India (67.52), State Bank of India (56.46) and Bank of Baroda (50.51).

d. Changes in Growth or Investment or Merged Banks

Investment refers to the investment of funds in the securities of another company/bank. They are long-term assets invested outside the business of firm. The main purpose of such investments is either to earn a return or/ and to control another company. It is usual that investments are shown in the assets side of balance sheet of banks. Further they are shown at market value. The investments are made in government securities, approved securities, assisted companies, subsidiaries/associates, mutual funds and others.

Table-6 portrays changes in average growth of investments and its variability of sample merged banks. It is significant to note that all the merged banks taken for this study have shown a tremendous growth in investments during post-merger period compared to the investments made during pre-merger period. The standard deviation brings out the fact that there is a higher variation in the growth of investment of all merged banks except State Bank of India during post merged than pre merged period. In the case of State Bank of India, the variation in the growth of investment is higher during pre-merged period. The analysis of t-test showed that out of seven merged banks taken for this study, all banks (State Bank of India, Oriental Bank of Commerce, Centurion Bank, Bank of Baroda and Union Bank of India, HDFC Bank and ICICI Bank) have significant 't' values. It is clearly understood from the mean growth rate of investment that ICICI Bank got high rate (1299.66) among sample banks. The low growth rate was achieved by State Bank of India (75.33).

e. Changes in Growth or Deposits or Merged Banks

The important element of conventional banking business is to accept deposits from the customers. Now-a-days manufacturing companies also started accepting deposits for short period from their members, directors and the general public. This mode of raising funds is popular on account of the fact that the bank credit becomes quite costlier. Deposit refers to deposits from public, (term deposits, savings bank deposits, demand deposits and miscellaneous deposits) and deposits outside India.

Table- 7 exhibits changes in average growth of deposits and its variability of sample merged banks. It is clear that all merged banks have shown a significant growth of deposits during post-merger period than the average deposits received during pre-merger period. It is true that the merger has led to the growth of deposits. The application of standard deviation proves that the variations in the growth of deposits of all banks during post merged period is higher than that of pre-merged period. The application of t-test showed that all merged banks have shown significant change in the average deposits after merger. The mean growth rate of deposits clearly shows the fact that HDFC Bank achieved (750.10) followed by ICICI (727.20), Centurion Bank (550.10), Oriental Bank of Commerce (149.04), Union Bank of India (75.39), State

Bank of India (68.45), and Bank of Baroda (68.14).

Improvement of Performance

The 't' value of different variables is given in Table-8. It is clearly understood that the average profits of Union Bank of India alone is insignificant. All other t-values for testing the equality of mean values with respect to total assets, revenue, investment and deposits are significant at 5% level. That is, the average of each variable has increased after the merger. This indicates that the goal of M&A activities is being achieved.

Conclusion

The present study analysed the growth of sample merged banks like State Bank of India, Oriental Bank of Commerce, Centurion Bank, Bank of Baroda, Union Bank of India, HDFC Bank and ICICI Bank during pre-merger and post merger periods. The above analysis clearly showed that the performance of merged banks in respect of growth of total assets, revenue, profits, investment and deposits was not different from the expectations. However, ICICI Bank has achieved higher growth rate in all respects (Except Deposit) among sample banks taken for the study. It is hoped by the corporate sectors that improved performance would follows M & A activities. If the banks want to proceed. with M & A activities, they have to proceed more carefully so that they can avoid the common mistakes associated with M & A activities. Further the banks may develop appropriate measures to gauge the success of the acquisition activities and adopt suitable measures to improve their post-merger performance in future also.

Table - 1

List of Sample Banks

S.No.	Name of the Bank	Year
1.	State Bank of India	1995
2.	Oriental Bank of Commerce	1997
3.	Centurion Bank	1998
4.	Bank of Baroda	1999
5.	Union Bank of India	1999
6.	HDFC Bank	2000
7.	ICICI Bank	2001

Table - 2

List of Merged Banks in India

S.No.	Merging Banks	Merged Bank	Year
1	Lakshmi Commercial Bank Ltd.	Canara Bank	1984
2.	Bank of Cochin Ltd.	State Bank of India	1984
3.	The Miraj State Bank Ltd.	Union Bank of India	1984
4.	The Hindustan Commercial Bank Ltd.	Punjab National Bank	1985
5.	Trader's Bank Ltd.	Bank of Baroda	1987
6.	United Industrial Bank Ltd.	Allahabad Bank	1988-89
7.	Bank of Tamilnadu	Indian Overseas Bank	1988-89
8.	The Bank of Thanjavur	Indian Bank	1988-89
9.	Parur Central Bank Ltd.	Bank of India	1988-89
10.	Purbanchal	Central Bank of India	1990
11.	New Bank of India	Punjab National Bank	1993
12.	Bank of Karad Ltd.	Bank of India	1994
13.	Kashinath Seth Bank	State Bank of India	1995
14.	Barl Doab Bank	Oriental Bank of Commerce	1997
15.	Punjab Co-Operative Bank	Oriental Bank of Commerce	1997
16.	20th Century Finance	Centurion Bank	1998
17.	Bareilly Corporation Bank	Bank of Baroda	1999
18.	Sikkim Bank	Union Bank of India	1999
19.	Times Bank	HDFC Bank	2000
20.	Bank of Madura	ICICI Bank	2001

Source: Business Today, Anniversary Iddue 2002, page. 92.

Table - 3

Changes in average Growth of Total Assets and its Variability in Select Merger Bank Unit

(Rs. in Crore)

S. No.	Name of the Banks	Mean		t-value	Growth Rate **
		Before	After		
1.	State Bank of India	95580.458 (15075.4644)	150652.93 (24051.7932)	3.880*	57.62
2.	Oriental Bank of Commerce	7374.6950 (2549.0112)	17416.475 (5594.2041)	3.267*	136.16
3.	Centurion Bank	458.8950 (576.1355)	3952.1650 (1978.9991)	3.390*	761.24
4.	Bank of Baroda	37257.253 (6311.1471)	61361.600 (7934.2772)	4.755*	64.70
5.	Union Bank of India	21430.078 (3632.3430)	37396.403 (5616.7544)	4.774*	74.50
6.	HDFC Bank	2496.9550 (1446.0069)	20412.480 (8393.8561)	4.207*	717.49
7.	ICICI Bank	6028.8950 (4583.7123)	89651.475 (47548.0968)	3.501*	1387.03

* - Significant level at 5%. ** - Mean growth rate.

Note: The figure given in the Parenthesis indicates SD.

Table - 4

Changes in average Growth of Profit and its Variability in Select Merger Bank Units

(Rs. in Crore)

S. No.	Name of the Banks	Mean		t-value	Growth Rate **
		Before	After		
1.	State Bank of India	192.2875 (70.2595)	1189.3850 (525.8260)	3.759*	518.54
2.	Oriental Bank of Commerce	82.2425 (70.8241)	224.7450 (41.3502)	3.475*	173.27
3.	Centurion Bank	6.7750 (7.6344)	21.9750 (11.5502)	2.196*	224.35
4.	Bank of Baroda	269.1325 (130.1746)	416.3900 (128.8793)	1.608*	54.71
5.	Union Bank of India	163.1825 (82.3834)	181.1175 (92.1703)	.290 (NS)	10.99
6.	HDFC Bank	51.5825 (26.9950)	253.7000 (114.8503)	3.426*	391.83
7.	ICICI Bank	64.7500 (28.6562)	815.6725 (722.5845)	2.077*	1159.72

* - Significant level at 0.05%. ** - Mean growth rate.

Note: The figure given in the Parenthesis indicates SD.

Table - 5

Changes in average Growth of Revenue Income and its Variability in Select Merger Bank Units.

(Rs. in Crore)

S. No.	Name of the Banks	Mean		t-value	Growth Rate **
		Before	After		
1.	State Bank of India	10306.640 (1508.3129)	16125.597 (2625.0234)	3.844*	56.46
2.	Oriental Bank of Commerce	793.1150 (259.2153)	1906.0100 (579.2368)	3.507*	140.32
3.	Centurion Bank	39,2375 (51.5081)	443.1425 (185.4030)	4.198*	1029.38
4.	Bank of Baroda	3996.5875 (532.6565)	6015.4725 (674.4929)	4.698*	50.51
5.	Union Bank of India	2245.7450 (428.3040)	3762.2050 (569.4494)	4.256*	67.52
6.	HDFC Bank	267.0025 (138.4182)	1690.8525 (726.3749)	3.851*	533.27
7.	ICICI Bank	564.5000 (365.9549)	6612.0750 (5263.7802)	2.292*	1071.31

* - Significant level at 0.05%. ** - Mean growth rate.

Note: The figure given in the Parenthesis indicates SD.

Table - 6

Changes in average Growth of Investments and its Variability in Select Merger Bank Units.

(Rs. in Crore)

S. No.	Name of the Banks	Mean		t-value	Growth Rate **
		Before	After		
1.	State Bank of India	26706.650 (8376.8134)	46825.635 (5834.1523)	3.942*	75.33
2.	Oriental Bank of Commerce	2645.7325 (845.8744)	7436.0500 (3089.8817)	2.991*	181.06
3.	Centurion Bank	97.0700 (147.8336)	1428.3350 (909.4827)	2.890*	1371.45
4.	Bank of Baroda	10604.825 (2084.6385)	19627.855 (3373.5032)	4.551*	85.08
5.	Union Bank of India	7383.0400 (1412.1015)	13175.165 (1749.9545)	5.152*	78.45
6.	HDFC Bank	1023.5325 (687.6139)	9573.0050 (3694.9577)	4.550*	835.29
7.	ICICI Bank	2184.1600 (1811.8388)	30570.778 (15290.8710)	3.687*	1299.66

* - Significant level at 0.05%. ** - Mean growth rate.

Note: The figure given in the Parenthesis indicates SD.

Table - 7

Changes in average Growth of Deposits and its Variability in Select Merger Bank Units.

(Rs. in Cror)

S. No.	Name of the Banks	Mean		t-value	Growth Rate **
		Before	After		
1.	State Bank of India	62822.413 (11724.5627)	105827.46 (19830.1043)	3.734*	68.45
2.	Oriental Bank of Commerce	6225.0325 (1927.7481)	15503.043 (5190.4078)	3.351*	149.04
3.	Centurion Bank	442.3733 (514.6854)	2878.0950 (1424.1396)	2.773*	550.60
4.	Bank of Baroda	31485.978 (5641.9816)	52941.170 (7116.8374)	4.725*	68.14
5.	Union Bank of India	19088.718 (3245.3444)	33480.735 (5034.8313)	4.805*	75.39
6.	HDFC Bank	1767.9050 (984.1820)	15028.928 (6213.1273)	4.216*	750.10
7.	ICICI Bank	4978.8925 (3820.5167)	41185.305 (22149.8285)	3.222*	727.20

* - Significant level at 0.05%. ** - Mean growth rate.

Note: The figure given in the Parenthesis indicates SD.

Table - 8

"T" Value of Different Variables.

S.No.	Name of Bank	Total Assets	Profit	Revenue	Investments	Deposits
1.	State Bank of India	S	S	S	S	S
2.	Oriental Bank of Commerce	S	S	S	S	S
3.	Centurion Bank	S	S	S	S	S
4.	Bank of Baroda	S	S	S	S	S
5.	Union Bank of India	S	N.S	S	S	S
6.	HDFC Bank	S	S	S	S	S
7.	ICICI Bank	S	S	S	S	S

Source: Computed from Table 3-7.

S : Significant

NS : Not Significant