Merger of Public Sector Banks in India- Synergies at Work

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1. Introduction

Mergers and Acquisition is a useful strategic tool for growth and expansion of Indian Banking Sector. It is helpful for survival of weaker banks by merging with the larger banks. In Public Sector Banks (PSBs) of India, majority stake (i.e. more than 51% of share capital) is held by government of India (www.rbi.org.in).There are a total of twenty one Public Sector Banks alongside one state-owned Payments Bank in India.

The Reserve Bank of India (RBI) / Government of India (GOI) evaluates public sector banks annually and rank them on performance parameters ranging from profitability to customer satisfaction. Last year, GOI had initiated its reforms agenda for state run lenders termed as EASE - Enhanced Access and Service Excellence - and directed them to draw up a board-approved strategic vision, consistent with their risk-appetite framework.

Various committees set up by RBI from time to time, {(Narasimham Committee (1998), Leeladhar Committee(2008), and Nayak Committee (2014)}, recommended for consolidation of Public Sector Banks (PSBs) in view of the following synergies-

a) Enhanced access to banking services,

b) Facilitate to create strong and competitive banks,

c) Catalysts for growth, with improve risk profile of the bank.

1.1 Reforms in 1991 - Recommendation of Narasimham Committee for Bank Merger

The Government of India setup a high level committee with Mr. M. Narasimham, Former governor of RBI, as Chairman of the committee to examine all the aspects related to structure, functions, organization and procedure of the financial system in India.

The Narasimham committee(1991) was setup to improve financial health of Public sector banks. So that these banks could be viable and meet fully emerging needs of the economy. The Narasimham committee(1991) recommendations aimed at ensuring a degree of operational flexibility, internal autonomy to the banks in their decision making process, and high level of professionalism in the banking operations.

The Committee proposed a substantial reduction in number of public sector banks through mergers and acquisition to improve greater efficiency in banking operations. They proposed a large pattern that consist of the following-

- Three to four large banks including SBI which could become international in character.
- Eight to ten national banks with a network of branches throughout the country engaged in general or universal banking.
- Local banks whose operations would be generally confined to a specific region.
- Rural banks including Regional Rural Banks (RRBs) whose operations would be confined to the rural areas and mainly engaged in financing of agriculture and allied services.

The banking reforms since 1992, based on the recommendations of Narasimham Committee (1991) aimed at transforming the highly regulated and directed system into one that is characterized by openness, competition and prudential supervisory discipline.

2. Literature Review

As per Rao & Kumar(2016), consolidation of business entities is a world-wide phenomenon. One of the tools for consolidation is mergers and acquisitions. The quest for growth and the ever-changing dynamic business environment makes Mergers and Acquisitions (M&A) a frequent phenomenon in corporate circles. The M&A in financial sector of India are driven with the objective of leveraging the synergies expected to arise out of the consolidation. The Indian banking sector has witnessed many M&A in the recent past. One of the major motives behind the mergers and acquisition in the banking industry is to achieve economies of scale and scope. This is because as the size increases the efficiency of the system also increases. Imala (2005) identified eight reasons for M&A in the financial services sector that includes:

a) Cost savings, attributable to economics of scale as well as more efficient allocation of resources;

b) Revenue enhancement, resulting from the impact of consolidation on bank size, scope, and overall market power;

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c) Risk reduction, due to change in organizational focus and efficient organizational structure;

d) New developments, which impose high fixed costs and the need to spread these costs across a large customer base;

e) The advent of deregulation, which removed many important legal and regulatory barriers;

f) Globalization, which engender a more globally integrated financial services industry and facilitated the provision of wholesale financial services and geographical expansion of banking operations;

g) Financial stability, characterized by the smooth functioning of various components of the financial system, with each component resilient to shock;

h) Shareholders' pressure on management to improve profit margins and returns on investment, made possible by new and powerful shareholder blocks.

So, these studies motivate to examine synergies at work after merging of public sector banks in India.

3. Previous Experiences of Mergers in Indian Banking System

Attempts to create an Indian bank that can be counted in the leading global banks are continuing since 1990. In February 2017,GOI approved merger of five associate banks with SBI and later merger of Bharat Mahila Bank. State Bank of Saurashtra was already merged with SBI in 2008, later in 2010; State Bank of Indore was also merged with it. Post merger, the SBI started process to rationalize its branch network by relocating some of the branches to maximize their reach and to optimize its operations and to improve their profitability.

Following mergers and acquisitions in Indian Banking system also have taken place:--

a) Merger of New Bank of India with Punjab National Bank

b) Acquisition of some small Private Banks with Public Sector Banks

c) ICICI Bank picked up Bank of Madura to get rural footprint and a footprint in the southern region with sizeable priority sector portfolio to attain National goals.

d) Kotak Mahindra Bank picked up ING Vysya bank to have business reach in the southern states.

It is pertinent to mention that in later cases there were wide cultural differences still synergies were created without value destruction.

4. Advantages of Merger to Banks

a) It can reduce the cost of banking operation.

b) It helps in broadening geographical reach of Banking.

c) It helps in leveraging on expertise of large Banks.

d) The scale of inefficiency of small banks can be minimized.

e) Larger size of the Bank can help to offer more products and services for its integrated growth of the Banking sector.

f) Large Bank can manage its short and long term liquidity better which helps in improving profitability.

g) The merged entity will have a larger capital base and dependency on Central Government to provide capital will be less.

h) Service conditions of Bank staff will be protected and therefore there will be no loss to them.

5. Present Merger Approval by Government of India

On 17.9.2018, GOI approved amalgamation of the three banks namely, Bank of Baroda, Vijaya Bank and Dena Bank. The proposed amalgamation will be a big positive for these lenders as it will ensure synergies for network, low-cost deposits and subsidiaries. The government proposes to achieve following objectives through this merger:

a) The amalgamated bank would be the third largest bank in India.

b) It will be a strong competitive bank with economies of scale.

c) It will create synergies for network, low-cost deposits and subsidiaries.

d) Customer base will be larger.

e) Wide Market reach.

f) Operational efficiency

g) Wider bouquet of products services for customers

h) Employees' interests will be protected.

i) Brand equity to be preserved.

j) All three banks are on the same software (Finacle CBS Platform)

k) Capital support will be ensured

The purpose of selecting the case of merger of three Public sector banks is to analyse the benefits of such consolidation to the concerned Banks, to the Government of India having majority stake and general customers availing banking services from these banks.

Let us now examine the merger case of BoB-Vijaya Bank--Dena Bank. The following are highlights of these three entities:

I. Vijaya Bank is one of the very few Banks that are showing profits while many other public sector Banks were showing losses.

II. Bank of Baroda showing losses in two of the last three years, but was able to absorb these because of its adequate capital.

III. Dena Bank is under the RBI's prompt corrective action (PCA) framework and is also barred from lending until it fixes its finances.

IV. Dena Bank has three years of losses;its business is not growing, and has got low productivity.

V. The approach of the government is to push a weak Dena Bank with a relatively strong Bank of Baroda (BoB) and to make it a strong Bank with the combined strengths of Vijaya Bank.

VI. Vijaya Bank has 52% of its branches in the southern region while Bank of Baroda (BoB) has only 10% of its branches in South, thereby giving the amalgamated entity a better footprint in the southern region of the country.

VII. Dena Bank has sizeable branches in Gujarat and Maharashtra, where Bank of Baroda (BoB) already has a very significant presence.

VIII. On its own, Bank of Baroda (BoB) is stronger in the Central and Northern Region.

6. Generation of Synergies

The amalgamation, approved by the Cabinet in September 2018, will create the country's third-largest Bank. This is in tune with the Govt.'s policy to have few but strong Banks with much larger balance sheet to support the rising appetite for credit of the fast-growing Indian economy. This will also ensure optimum utilization of resources. RBI shall provide regulatory inputs and capital needs of the larger entity once the merger is implemented.

The data presented in this section on some of the areas will highlight how proposed merger of three Banks shall be beneficial to all the stake holders:-

Table 1: Shareholding Pattern of GOI in Merging Banks (as on 31 Mar, 2018)

Bank Name	Total Government & RBI– Resident	Financial Institutions - Resident	Financial Institutions- Non- Resident	Other Corporates - Resident	Other Corporates- Non-Resident	Total Individual - Resident	Total Individual- Non-Resident	Total – Resident	Total – Non-Resident
BOB	64.0	14.0	13.9	1.9	-	5.6	0.4	85.6	14.4
DENA BANK	80.7	1.7	-	9.6	1.2	6.5	0.2	98.5	1.5
VIJAYA BANK	68.8	18.6	-	1.9	-	10.2	0.5	99.5	0.5

Source: RBI Report on Trend and Progress of Banking in India 2017-18

As evident from table 1, the Government of India & RBI shall have more than stipulated 51% share in the capital of the merged entity, so there may not need any further capitalization by the Government of India to the merged entities if capital adequacy norms are met

Table 2: Number of Bank Branches of Merging Banks (as on June, 2018)

Sr. No.	Name of the Bank	Branches				
		Rural	Semi - Urban	Urban	Metropolitan	Total
1	Bank of Baroda	1,836	1,537	932	1,169	5,474
2	Dena Bank	573	433	368	418	1,792
3	Vijaya Bank	514	546	535	540	2,135
	TOTAL	2923	2516	1835	2127	9401

Source: RBI Report on Trend and Progress of Banking in India 2017 -18

Total number of merged entity will have approximately 9400 branches as per table 2, which will be second highest in the country after State Bank of India. This will ensure reach of the merged Bank to every nook and corner of the country, and shall present enough scope for merging and re-locating their branches purely on commercial needs and for optimal utilization of internal resources. The newly merged entity will have the second highest number of branches across the country which is next to State Bank of India (SBI) having highest number of branches at 22,414.

Table 3: Overseas Operations of Merging Banks (as on March, 2018)

Sr. No.	Name of the Bank	Branches	Representative Office	Subsidiary	Joint Venture	Other Offices	TOTAL
1	Bank of Baroda	50		9	2	9	70
2	Dena Bank	--	1	--	--	--	1
3	Vijaya Bank	---	---	---	---	---	---

Source: RBI Report on Trend and Progress of Banking in India 2017-18

It is evident from table 3 that only Bank of Baroda has got more overseas operations. Now with more internal resources and solid capital base the merged entity will be able to further spread their wings across the globe.

Table 4: Number of ATMs of Merging Banks (as on June, 2018)

Sr. No.	Name of the Bank	ATMs		
		On-site	Off-site	Total
1	Bank of Baroda	6,263	3,352	9,615
2	Dena Bank	1,326	320	1,646
3	Vijaya Bank	1,678	493	2,171
TOTAL		9,267	4,165	13,432

Source: RBI Report on Trend and Progress of Banking in India 2017-18

The ATMs have become bare minimum need of every Bank customer. The merged entity will have more than 13000 ATM machines across the country as per table 4, which will again be second highest amongst all Banks operating in India. This will further help them to serve their customers at various places and will enable the Bank to consolidate on economic reasons.

Table 5: Business Figures of Merging Banks (as on March, 2018)

Sr. No	Name of the Bank	DEPOSITS (Rs. in Crores)	ADVANCES (Rs. in Crores)
1	Bank of Baroda	5,91,314	4,27,432
2	Dena Bank	1,06,130	74,239
3	Vijaya Bank	1,57,287	1,16,165
TOTAL		8,54,731	6,17,836

Source: Financial reports accessed from www.bankofbaroda.in, www.denbank.com,www.vijayabank.com(as on 31-03-2018)

Table 6: Capital and Non-Performing-Assets of Merging Banks (as on March, 2018)

Sr. No	Name of the Bank	Capital Ratio (CRAR) (%) BASEL--III	Gross NPAs (Closing Balance) (Rs. in Crores)	Net NPAs to Net Advances (%)
1	Bank of Baroda	12.13%	56480.38	5.49%
2	Dena Bank	11.09%	16,361	11.95%
3	Vijaya Bank	13.90%	7526	4.10%

Source: Published financial report on respective bank's website (as on 31-03-2018)

According to the government's estimates, net non-performing assets (NNPA) ratio of the combined entity will be at 5.71 percent as per table 6, which will be significantly better than public sector banks (PSBs) average of 12.13 percent. Also, Capital Adequacy Ratio (CRAR) will be at 12.25 percent, which will be significantly above the regulatory norms.

Table 7: Profitability Parameters of Merging Banks (as on 31 March, 2018)

Sr. No	Name of the Bank	Net Profit/Loss	Net interest margin%	Cost of deposit%
1	Bank of Baroda	-2432	2.43%	4.56%
2	Dena Bank	-1923	2.19%	5.62%
3	Vijaya Bank	727	3.10%	5.65%

Source: Financial report on respective bank's website (as on 31-03-2018)

It is pertinent to observe from table 7, that two out of three Banks are having accumulated losses. It is therefore a fit case of merger as the combined entity will have more scope for covering these losses. The positive aspect about all three Banks is their good net interest margin and low cost of funds. This will pave the way for their profitability in the next financial year.

Table 8: Staff Strength of Merging Banks (as on March, 2018)

Sr. No	Name of the Bank	Total Staff Strength
1	Bank of Baroda	56,361
2	Dena Bank	13,613
3	Vijaya Bank	16079

Source: Financial reports accessed from www.bankofbaroda.in, www.denbank.com,www.vijayabank.com

(as on 31-03-2018)

The employee strength of the new entity would be over 84,000 as per table 8, after the merger as on March 2018.The merger will not cause any job loss in any of these banks and, as was in case of SBI, no employee of the three banks would have service conditions that are adverse to their present one

7. Discussion

Banking in India, especially Public Sector Banks are passing through a very critical phase. While on one hand the high non-performing assets are a cause of concern, the capital adequacy norms are becoming stricter day by day on the other hand.

Mergers between Public Sector Banks naturally resolve many issues. The foremost being that it reduces the unhealthy competition and ensures better utilization of financial resources. The merged entities shall have larger reach and the operational cost comes down automatically. This will result in considerably higher savings and profits.

The various parameters discussed above clearly manifests these issues for merger of the said three Banks.The merged entity may face challenges on business integration, technology, culture and people management and a possible opposition by trade unions.

8. Limitations and scope for future research

This study is based on analysis of secondary data (Published Financial report of banks & yearly consolidated data by RBI) and experience of authors. Therefore the study is limited to only one aspect of merger of Banks and synergies created by it. The other aspect like views of the bank customers, bank staff etc. though important but have not been taken up in this study. Secondly, the study is confined to only some important financial parameters of banking, it does not include non-financial aspects of merger of Banks, like merger of database of three different entities, merging of systems and procedures of different banks, adoption of uniform documentation by these Banks and adoption of similar stationary by the merged entity. The study has also not taken into account the inconvenience that may cause to bank customers due to abrupt merger of banks, which includes their personal relationship with the bank staff and ease of doing business with the bank.

The study has also not taken into account legal hurdles in the merger from the affected parties, including staff unions/associations point of view and their bargaining power as regards staff benefits and perks.Therefore, authors do not claim that the study is complete, final and foolproof.

There is enough scope for widening the area of Bank merger. In the following areas further research can be done:--

1. Impact of merger on customer loyalty.
2. Non-financial aspects of Bank merger.
3. Inconvenience caused to the Bank customers due to operational issues.
4. Opinion of Bank staff unions & officer associations.
5. Problems faced and solved by the Bank operational staff after merger.
6. Change of policy guidelines by Banks on merger.

9. Conclusion

As banks merge together, their area of operation will become wider and not limited to one state or one part of the country. With adoption of best of the work culture amongst the merged banks, work efficiency and effectiveness shall become visible. With a bigger workforce and enriched Management there will definitely implementation of best corporate governance practices.

Higher workforce will also lead to the scope of utilizing them for new areas and new places. The management shall be better and sufficient resources will be available for further improvement of the infrastructure and providing skill based training for development of employees.

There are many PSBs which are running in losses and their financial position is under strict vigilance of the regulators. The merger of these three banks can well be treated as a stepping stone for more mergers in near future to create synergies in the banking industry.

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