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Mergers and Acquisitions in Selected Banks in India

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Abstract

Banks have played an essential role in the economy. Banks encourage the saving habits among the people and circulate the funds from excess to where they needed. Banks provide economic development as well as different employment opportunities. This research paper is based on the banks performance while they acquire another bank or another bank merges with them. This research study is exploratory and descriptive in nature. Secondary data has been used for completion the study. Various statistical tools have been significantly used like mean, standard deviation, t-test, etc. to find some meaningful results. The main objective of the study is to find the banks performance, profitability and effect of merger.

Key Words

Purpose of Merger & Acquisition, Pre and Post Merger Performance, Profitability Analysis, etc.

INTRODUCTION

Banks facilitate the growth of an economy. Main activity of the banks is to collect the surplus funds and lend this fund to household, business group, etc for consumption and investment purpose. Banks can be called as the backbone of any nation that make easier the financial transactions, development the farming and backward sector by providing them the financial assistance and enhance the standard of living of the society by providing them loans. In present scenario, different

banks are also enhancing their business size by capturing another banks i.e. merger or acquisition. Merger is the combination of different business entities to become a single entity while acquisition shows the purchase of controlling interest of one entity by the other entity. Due to privatization in banking sector these kinds (merger or acquisition) of banking growth & expansion activities are increasing. The present study also focuses on the merger and acquisition in banking sector. The basic purpose of the merger & acquisition are to achieve the faster economic growth and improvement before their competitors. Tambi (2005) examined the impact of merger on the performance of a corporation of India. However, the theoretical assumption says that merger improves the overall performance of the corporation due to increased market power. This study evaluated the performance of some banks and proved that merger have failed to contribute positively. Although, merger & acquisition are performed to obtain the safeguard in competition, to achieve economies of scale, to improve quality & strengthening the business status, to obtain new business options, to diversification of business activities, etc. After the nationalization of the banks mergers & acquisitions have been significantly raised. From last few years, different banks are choosing this process to expand their business size by capturing the business of another bank.

REVIEW OF LITERATURE

Before moving ahead it is very important to understand the literature which gives the direction to the study by providing the understanding of already studied parameters and tools & techniques for completion the present study. Lubatkin (1983) studied that the merger provides real benefits to the acquiring firms and resulted that acquiring firm benefited by mergers & acquisitions. Revenscraft and Scherer (1987) analyzed in their study the merger of 450 US companies during 60s-70s and found that market share and profitability of most of companies declined.

Healy *et al.* (1992) examined the post merger performance of 50 largest US mergers in between 1979 and 1984 and proved that operating performance of merging firms improved after merger in comparison of other firms in industry. Berger (1998) concluded in the study that very little improvement in cost efficiency for merger and acquisition for both large and small banks. Mishra and Chandra (2006) concluded that mergers & acquisition not have any significant impact on profitability of the firm in long run. Schiereck Dirk *et al.* (2009) studied the relationship between bank reputation after mergers & acquisitions and its effect on shareholder's wealth. This study covered 285 European mergers & acquisitions in between 1997-2002 and

proved that the average wealth not significantly affected by mergers & acquisitions. Antony Akhil (2011) researched the impact of the banks merged in between 1999-2011 & 18 mergers & acquisitions took place in Indian banking sector. With the use of pared t-test this study proved that there is a significant difference in the profitability ratio of the bank after merger. Sharma & Warne (2012) studied the pre and post merger impact on share price fluctuations. This study was exploratory and descriptive. This research specially focused on the impact of merger on ICICI bank Ltd and proved that there is no significant price benefits was gained from the merger.

RESEARCH METHODOLOGY

Research methodology plays a significant role for the completion of the research work. The present study is descriptive and exploratory in nature. For the completion of the research work secondary data has been used. There are only three banks which have been studied (ICICI Bank, Bank of Rajasthan Ltd., Bank of Madura). The present study is categorized into two cases one case to understand merger impact and the another case to judge the impact of acquisition. Various tools and techniques are significantly adopted for result findings.

OBJECTIVES OF THE STUDY

- To study bank's pre-post merger/acquisition effect on net profitability.
- To evaluate the pre-post performance in terms of debt-equity ratio.
- To evaluate the pre-post performance in terms of return on capital employed.
- To analyze the pre-post effect of merger/acquisition on equity shareholder.

STATISTICAL TOOLS AND TECHNIQUES

For the completion of the present research study some statistical tools like as mean, standard deviation, t-test and various profitability ratios (gross profit ratio, net profit ratio, operating profit ratio, debt-equity ratio, return on capital employed, etc.) has been significantly used for result findings.

LIMITATIONS OF THE STUDY

The present study is based only on three banks. Secondary data has been used so limitations of secondary data also covered in this study.

Data Analysis and Findings

Table 1 and 2 both are showing the merger impact of ICICI bank and bank of Rajasthan i.e. on August, 13, 2010. As shown in table 1 the financial and accounting ratios have been significantly calculated. Gross profit margin of bank of Rajasthan is decreasing and of ICICI bank is increasing. By comparing other

Table 1

Merger of ICICI Bank and Bank of Rajasthan

	Bank of Rajasthan			ICICI Bank		
	2007	**2008**	**2009**	**2007**	**2008**	**2009**
Gross Profit Margin	17.26	14.19	11.43	12.17	12.46	12.79
Net Profit Margin	12.37	09.57	7.77	10.38	10.28	9.40
Operating Profit Margin	50.85	38.85	34.03	45.39	42.11	43.18
Debt-equity Ratio	0.75	0.65	0.46	2.93	1.87	1.88
Return on Equity	25.94	21.75	18.29	12.64	8.88	7.59
Return on Capital Employed	14.82	13.20	12.53	3.26	3.12	2.63

Source : PROWESS

Table 2

Combined Mean and Standard Deviation of Pre-merger and Post-merger Ratios of ICICI Bank and Bank of Rajasthan

		Mean	**S.D.**	**t-value**	**Sig.**
Gross Profit Margin	Pre	13.48	1.46	0.2392	0.139
	Post	19.26	2.75		
Net Profit Margin	Pre	9.95	1.39	-2.357	0.143
	Post	14.43	1.99		
Operating Profit Margin	Pre	42.40	5.03	-1.569	0.257
	Post	46.90	1.88		
Debt-equity Ratio	Pre	1.42	0.36	-1.838	0.207
	Post	2.04	0.24		
Return on equity	Pre	16.51	4.30	2.185	0.161
	Post	9.28	1.45		
Return on Capital Employed	Pre	8.17	0.85	8.153	0.015
	Post	3.03	0.24		

Source : Processed by MS Excel Level of Significance – 5%

ratios it is proved that bank of Rajasthan is going in decreasing year by year. Likewise data stated in table 2 proved that the performance of ICICI bank has not improved after merger in terms of return on capital employed, return on equity and resulted the statistically significant difference after the merger.

Table 3

Acquisition of ICICI Bank and Bank of Madura

	Bank of Madhura			ICICI Bank		
	1997	**1998**	**1999**	**1997**	**1998**	**1999**
Gross Profit Margin	10.06	11.53	9.18	23.55	20.29	14.53
Net Profit Margin	8.73	9.24	7.14	17.65	14.45	9.85
Operating Profit Margin	43.56	45.85	39.50	48.48	45.65	33.80
Debt-equity Ratio	2.3	0.58	1.4	0.54	0.72	1.19
Return on Equity	21.15	22.32	16.99	22.06	18.83	20.55
Return on Capital Employed	6.41	14.15	7.09	14.30	10.94	9.37

Source : PROWESS

Table 4

Combined Mean and Standard Deviation of Pre-Post Acquisition Ratios of ICICI Bank and Bank of Madura

		Mean	S.D.	t-value	Sig.
Gross Profit Margin	Pre	14.85	2.63	2.997	0.096
	Post	10.71	4.59		
Net Profit Margin	Pre	11.17	2.41	1.027	0.413
	Post	9.97	0.86		
Operating Profit Margin	Pre	42.97	5.47	1.578	0.255
	Post	41.21	3.56		
Debt-equity Ratio	Pre	1.12	0.41	-1.651	0.240
	Post	5.60	4.34		
Return on equity	Pre	20.31	1.43	2.246	0.154
	Post	10.95	6.83		
Return on Capital Employed	Pre	11.37	3.76	2.400	0.0138
	Post	3.06	3.08		

Source : Processed by MS Excel Level of Significance – 5%

Table 3 and 4 stated the financial and accounting profile of bank of Madura and ICICI bank. Table 3 representing that GP margin is decreasing of both the banks. Increase in debt-equity ratio of ICICI bank, Decrease in return on capital employed also. Table 4 highlighting no change in ICICI bank net profit margin after acquisition, return on capital employed is increased and ICICI's performance is improved in relation to return on equity.

CONCLUSION

Mergers & acquisition have some positive and negative impacts. In the present study after analyzing the financial and operating parameters to judge the performance of ICICI bank after merger with bank of Rajasthan and acquisition with bank of Madura. Some parameters have changed but some not. But the present study focused only on three years it may occur ICICI bank may gain the benefits later. The financial performance of ICICI bank has been improved after the merger case with bank of Rajasthan. Profitability performance improved but return on capital, return on equity has not improved. But in second case during the course of acquisition of bank of Madura the data analysis not showed any significant change in the ICICI bank profile. No change shown in net profit margin and adverse impact on return on capital.

For further research in this area data for more years can be used to find more meaningful results as well as by using some other statistical tools and techniques to explore the great depth of the mergers and acquisition cases.

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