

Strategic Dynamics in the Indian Banking Sector: An In-depth Analysis of Mergers and Acquisitions for Sustainable Economic Growth

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Abstract

One of the main components of a robust economy is an effective and stable banking system. India's unique geographic, social, and economic characteristics set it apart from other Asian nations in terms of banking systems. The banking sector contributes significantly to the Indian economy by obtaining deposits from all socioeconomic sectors and making timely loans to all of them. In India, commercial banks facilitate equitable regional development by furnishing the necessary financial resources and infrastructure to underserved areas. Additionally, they motivate people to save their money and invest it in productive ventures, which promotes economic growth and greatly improves employment opportunities. The banking sector in India is growing rapidly in recent years, changing its structure through mergers and acquisitions. Its main goals are to maintain strong financial health, manage the increase in non-performing assets or bad loans, upgrade technology, and guarantee greater scale efficiency. Investigating the operation of notable mergers and acquisitions in the Indian banking industry is the aim of this study. It is imperative that the Indian banking system be integrated through mergers and acquisitions that are motivated by business strategies and considerations. The merging of banks fosters global expansion and heightened synergy, allowing larger financial institutions to acquire distressed assets from their smaller counterparts. The current study adopts this approach so as to better understand the rationale behind bank mergers and acquisitions, and also the consequences of these transactions on the equity shares of shareholders' capital and the participating banks' financial performance.

Keywords- Mergers and Acquisitions, Indian Banking Sector, Stakeholders, Equity Shares, Synergy, Financial Performance.

Introduction

In today's intensely competitive landscape, expansion is the norm. Organizations can achieve growth through internal means, such as broadening activities and setting up additional branches, as well as through various strategies like mergers and acquisitions (M&As), takeovers, amalgamations, joint ventures, and more. Mergers and acquisitions stand out as the dominant long-term approach for enhancing and reorganising businesses in the modern, globalized world, especially amid the intensifying daily rivalry. Like all other business organizations, banks have to be cautious about potential threats and seize opportunities presented by both present and emerging trends. In response to a dynamic environment, the banking sector is resorting to corporate reorganization, consolidation, and strengthening as means of

maintaining effectiveness and sustainability. As a result, the preferred strategy for growing banks' size is mergers and acquisitions, which has a big impact on their capacity to join the global financial system. A bank acquisition happens when a company buys another. The smaller bank joins with the larger bank, losing its status as a separate legal organization. The bank might keep operating under its original name or it may merge with the bigger bank, contingent on the terms of the deal. Bank mergers strengthen the organization's ability to survive in the fast-paced business world. Through mergers, the weaker banks can grow in the local and international financial markets and quickly adapt to shifting market conditions. The question of whether bank mergers within Indian banking sector should be considered new developments currently arises. This worry can be allayed by the fact that bank mergers have long existed in the Indian financial sector. In India, bank mergers have been commonplace since before the country's independence. The Bank of Bengal, Bank of Bombay, and Bank of Madras merged into the State Bank of India in 1921, marking the first merger of banks in Indian history. Mergers and acquisitions have a favourable financial effect on the banks and also on the country's economy. The expectations and preferences of today's corporate clients are evolving, which is putting banks under pressure to review their processes and create entirely new technology to meet their needs. In India, the financial system is severely restricted by the government, which denies it the independence necessary for continuous development, mechanical advancement, and intense competition. In these situations, consolidation strategies such as mergers and acquisitions (M&A) become one of the foremost approaches to obtain the upper hand.

The following are the latest bank mergers in the Indian banking industry:

Date	Merging Banks	Merged with
April 1, 2020	Allahabad Bank	Indian Bank
	Andhra Bank and Corporation Bank	Union Bank of India
	Oriental Bank of Commerce and United Bank of India	Punjab National Bank
	Syndicate Bank	Canara Bank
April 1, 2019	Dena Bank and Vijaya Bank	Bank of Baroda
April 1, 2017	State Bank of Bikaner & Jaipur, State Bank of Mysore, State Bank of Patiala, Bhartiya Mahila Bank, State Bank of Travancore, State Bank of Hyderabad.	State Bank of India

The Necessity of Bank Mergers and Acquisitions

The mergers and acquisitions (M&A) in the banking sector are influenced by different strategic, financial, and regulatory factors. Here's a detailed breakdown:

- **Economies of Scale and Scope:**
- **Cost Efficiency:** Combining operations often leads to economies of scale, lowering per-unit costs. This can include shared infrastructure, technology, and administrative functions.

- Diversification: Banks that merge can expand the range of products and services they offer. This reduces risk exposure to specific sectors or regions.
- **Market Share and Competitiveness:**
- Market Dominance: Mergers and acquisitions can increase a bank's market share, enhance its competitiveness, and give it a stronger edge in negotiations with customers and suppliers.
- Global Presence: Acquiring a bank may allow the buying entity to enter new markets or strengthen its global reach.
- **Technological Advancements:**
- Digital Transformation: Buying a technologically advanced bank can speed up digital transformation efforts. It helps traditional banks respond to changing customer preferences and technological trends.
- **Risk Management:**
- Diversification of Risks: M&A allows banks to spread risks across a wider range of assets. This can be key in reducing the impact of economic downturns or sector-specific challenges.
- **Regulatory Compliance:**
- Meeting Regulatory Requirements: Mergers can arise from changes in regulations or requirements, such as stricter capitalization standards. Consolidation helps banks meet these demands more effectively.
- **Enhanced Financial Performance:**
- Profitability: Synergies from M&A can lead to better financial performance through increased revenue generation and cost savings.
- **Customer Base and Relationships:**
- Expanded Customer Base: Mergers allow banks to gain a larger customer base, which can lead to more cross-selling opportunities and revenue sources.
- Customer Retention: A well-managed M&A can improve customer satisfaction and retention. This happens by maintaining existing services while introducing new and better offerings.
- **Access to Talent:**
- Human Capital: Acquiring banks often gain skilled personnel, including specialized experts in finance, risk management, and technology.
- **Financial Strength:**
- Capital Infusion: Mergers can provide a boost of capital, improving the financial condition of the combined entity. This is especially vital during economic downturns or financial crises.
- **Strategic Positioning:**
- Strategic Focus: M&A allows banks to refine their strategic goals and positioning in the market, creating a more focused and competitive organization.

While M&A activities can provide many benefits, successful execution requires careful planning, thorough assessment, and effective integration strategies to achieve the expected synergies. Moreover, challenges like cultural differences, regulatory obstacles, and execution risks must be managed effectively.

Review of Literature

(Adhikari et al., 2023) advises commercial banks to engage in mergers and acquisitions (M&A) with other commercial banks as opposed to smaller development banks and financing firms in order to increase their competitiveness, cost effectiveness, and risk diversification. Moreover, this study stipulates that the

weaker BFIs do not yield positive consequences on the merger related to commercial banks. Hence, the NRB should promote commercial banks to seek suitable partners rather than compelling the merger of two smaller, less robust commercial banks. Additionally, the NRB should actively facilitate the merger of commercial banks backed directly and indirectly by single-family homes or business groups, and also those with cross-holdings. This is essential to establish financial stability and uphold corporate governance within the country's financial institutions (BFIs).

Srivastava Nidhi et al. (2022) emphasised on the mergers and acquisitions (M&A) that have occurred in the financial sector in India under the title "A Study of Mergers and Acquisitions in Indian Banking Sector." The study's conclusions showed that by removing barriers to reinforcement, the current formative banking techniques are making room for a more straightforward framework. It added that merging two strong banks can generate the type of synergy required to enable them to compete globally. The researchers conclude that there's a chance that different banks are impacted by M&A performance in different ways. Whereas, a disastrous merger could cause business operations to be disrupted, client confidence to decline, the company's credit to suffer, representatives to depart, and employee inspiration to drop.

Yadav, 2022 concluded that although the profit from the purchase and merger of Indian banks has occurred, it has not occurred to the extent that we had anticipated. So, to make more money, we need to explore the areas where issues still exist. What causes these issues, and why must they be identified and fixed so as to maximize their advantages? Recently, there have been many mergers and acquisitions within the banking sector (PSB). This will facilitate the organization's rapid growth and expansion as well as its instant acquisition of a sizable clientele.

Sengar et al., 2021 attempted to use a case study to study the issue of post-merger performance analysis based on a qualitative approach. The performance before the merger and after the merger are illustrated using the SWOT Analysis technique. The acquirer bank has surpassed its rival bank to become the largest employer in the private banking industry with the inclusion of more than 10,000 positions during the latest fiscal year. This study's qualitative analysis leads it to the conclusion that bank mergers are successful and beneficial for all parties that are involved, including the shareholders and clients of the acquired bank and also the newly formed acquirer company. The acquisition strengthens the acquirer bank's position in the Indian market and branch network.

Musah et al., 2020 looked into how mergers and acquisitions affected Ghanaian commercial banks' net profit margin, return on equity, and return on assets. Despite the lack of a clear conclusion, the data showed a substantial and negative correlation between mergers and acquisitions and net profit margin. Return on equity showed a negative but statistically irrelevant relationship, and return on assets showed a positive but statistically irrelevant relationship. There is insufficient evidence in the study to conclude that mergers and acquisitions enhance bank performance in Ghana. However, larger banks showed a strong correlation with improved financial performance, lending credence to the concept of economies of scale. In order to improve profitability after a merger, the study advises businesses to implement cost-cutting measures. It also supports further research on performance metrics like asset quality and liquidity.

The reasons and effects of bank mergers in the Indian economy were the primary topics of *B Ravi (2019)* study, "Recent Mergers and Acquisitions in Indian Banking Sector-A Study." According to this study, the merger's main objective is to accelerate business growth. It added that the company could safeguard its sources of raw materials through mergers and acquisitions and attain purchasing efficiencies like cost savings on transportation, lower overhead for the buying department, etc. According to this study, a company's size can help it remain competitive in the fast-paced business environment that values agility,

speed, and customer responsiveness. As a recognized strategic justification for the same, mergers and acquisitions (M&As) as a method of boosting competitive power become more prominent in this context. In their research, *Singh and Das (2018)* evaluated the effect of mergers and acquisitions on the financial performance of Indian banks. The purpose of this paper was also to ascertain how security prices were impacted by merger and acquisition announcements made while the study was going on. This research depends on secondary data for its study foundation. As per the findings of the study, the market initially tried to react negatively to the news that the majority of banks were undergoing acquisition. Nevertheless, for shareholders in both public and private sector banks, the outcome typically involved either the creation or destruction of wealth. According to this study, the employees of the combined banks who were still in business had positive opinions about the merger that their company had carried out. Employees were initially suspicious when they got to know about the merger, but management communication made it easier for them to get used to the unfamiliar circumstances. The staff started to comprehend the rationale of the merger plan and developed trust in their organization as an outcome of being included in the transformational process.

Objectives of the Research

The primary objectives of this study are as follows:

1. Elucidate the imperative rationale driving bank mergers and acquisitions.
2. Scrutinize the repercussions of mergers and acquisitions on the shares of the pertinent bank and the equity components of shareholders' capital.
3. Delve into the discernible effects of mergers and acquisitions on the financial performance of the Indian banking sector.

Methodology of the Research

This study uses secondary data. The Reserve Bank of India's publications, the bank's public annual reports, and a variety of websites that offer various data on the banks selected as a sample were the sources of the relevant information used to investigate the impact of mergers and acquisitions on the sample banks' financial performance.

For this study, a sample of six merger and acquisition cases from the banking sector in India was selected. These cases include the M&A of Allahabad Bank with Indian Bank, Andhra Bank & Corporation Bank with Union Bank of India, Oriental Bank of Commerce & United Bank of India with Punjab National Bank, Canara Bank with Syndicate Bank, Bank of Baroda with Dena Bank & Vijaya Bank, State Bank of India with State Bank of Mysore, State Bank of Patiala, State Bank of Bikaner & Jaipur, State Bank of Travancore, State Bank of Hyderabad and Bharatiya Mahila Bank.

The net profit ratio, return on equity, earning per share, return on assets, and return on equity were the main financial metrics employed in this research to know the financial performance of the participating banks pre- and post-merger. For the investigation, the average financial ratios were computed for the three years leading up to and the three years succeeding the merger.

Data Analysis and Interpretation

Return on Assets: A company's net, after-tax income is divided by the total value of its assets to ascertain the Return on Assets (ROA) ratio. It's necessary to note that because banks are so highly leveraged, a bank

may still have substantial revenues and profits even with a ROA of 1% to 2%. The following table displays the banks' return on assets as a result of this study:

Table 1: Return on Assets

Name of the Bank	Year of Merger	Return on Assets (in %)					
		Pre-Merger			Post-Merger		
		31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022	31-03-2023
1. Indian Bank	April 1, 2020	0.49	0.11	0.24	0.47	0.58	0.74
2. Union Bank of India	April 1, 2020	-1.07	-0.59	-0.52	0.27	0.44	0.65
3. Punjab National Bank	April 1, 2020	-1.60	-1.28	0.04	0.16	0.26	0.17
4. Canara Bank	April 1, 2020	-0.68	0.04	-0.30	0.22	0.46	0.78
		31-03-2017	31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022
5. Bank of Baroda	April 1, 2019	0.19	-0.33	0.05	0.04	0.07	0.56
		31-03-2015	31-03-2016	31-03-2017	31-03-2018	31-03-2019	31-03-2020
6. State Bank of India	April 1, 2017	0.63	0.42	0.38	-0.18	0.02	0.36

(Source: Annual Reports, Ministry of Corporate Affairs)

The aforementioned table depicts that subsequent to their merger and acquisition, the return on assets of Indian Bank, Union Bank of India, PNB, and Canara Bank greatly increased; in contrast, the ROA of the Bank of Baroda hardly changed in the first two years after the merger but has shown significant increase in the third year. The table unequivocally demonstrates that SBI's return on assets (ROA) was greater before the merger than it was afterward.

Return on Equity: The balance sheet and income statement are combined to create return on equity (ROE), a two-part measure of financial performance. It is thought of as a gauge of how profitable and successful an organization is at turning a profit. Profitability of a bank can be computed by dividing its net income by the equity held by its shareholders; the higher the number, the higher the return. The study's return on equity for the banks in question is displayed in the table below:

Table 2: Return on Equity

Name of the Bank	Year of Merger	Return on Equity (ROE) in %	
		Pre-Merger	Post-Merger

		31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022	31-03-2023
1. Indian Bank	April 1,2020	7.95	1.97	3.94	11.88	10.52	12.61
2. Union Bank of India	April 1,2020	-20.90	-12.15	-9.46	4.87	7.94	11.68
3. Punjab National Bank	April 1,2020	-32.85	-24.20	0.58	2.41	3.90	2.74
4. Canara Bank	April 1,2020	-14.51	1.16	-6.78	5.05	9.85	16.03
		31-03-2017	31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022
5. Bank of Baroda	April 1, 2019	3.43	-5.60	0.94	0.76	1.07	8.46
		31-03-2015	31-03-2016	31-03-2017	31-03-2018	31-03-2019	31-03-2020
6. State Bank of India	April 1,2017	10.20	6.89	6.69	-3.37	0.39	6.95

(Source: Annual Reports, Ministry of Corporate Affairs)

The table above shows that following mergers and acquisitions, the return on equity of the Indian Bank, Union Bank of India, PNB, Canara Bank, and Bank of Baroda all increased considerably. However, the State Bank of India's return on equity, which was greater prior to the merger (i.e., 10.20), changed from being positive to negative after the merger to being positive again during the subsequent fiscal years.

Net Profit Ratio: Also known as the net profit margin ratio, the net profit ratio gauges the funds generated by a business relative to its earnings. In other words, the connection between a company's net profit margin and net sales is reflected in the net profit margin ratio. The net profit ratios for the relevant banks, as per this investigation, are presented in the table below:

Table 3: Net Profit Ratio

Name of the Bank	Year of Merger	Net Profit Ratio (in %)					
		Pre-Merger			Post-Merger		
		31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022	31-03-2023
1. Indian Bank	April 1,2020	7.35	1.67	3.51	7.68	10.15	11.75
2. Union Bank of India	April 1,2020	-16.02	-8.65	-7.78	4.22	7.70	10.44
3. Punjab National Bank	April 1,2020	-25.59	-19.44	0.62	2.50	4.61	2.94

4. Canara Bank	April 1, 2020	-10.23	0.74	-4.56	3.69	8.18	12.56
		31-03-2017	31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022
5. Bank of Baroda	April 1, 2019	3.27	-5.57	0.87	0.71	1.17	10.40
		31-03-2015	31-03-2016	31-03-2017	31-03-2018	31-03-2019	31-03-2020
6. State Bank of India	April 1, 2017	8.59	6.06	5.97	-2.96	0.35	5.63

(Source: Annual Reports, Ministry of Corporate Affairs)

The net profit ratios of the Union Bank of India, PNB, Indian Bank, Canara Bank, and Bank of Baroda all exhibit a positive change following mergers and acquisitions, as demonstrated by Table No. 3. In contrast, SBI's net profit ratio was more before the merger (i.e., 8.59), turned negative following mergers and acquisitions, and then turned positive again in the subsequent fiscal years.

Earnings Per Share: Earnings per share is the amount of money an organization makes for each outstanding share of common stock. It is commonly used to determine stock price and is an essential measure of organizational profitability.

Table 4: Earnings Per Share

Name of the Bank	Year of Merger	Earnings Per Share (in Rs.) [Basic EPS]					
		Pre-Merger			Post-Merger		
		31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022	31-03-2023
1. Indian Bank	April 1, 2020	26.21	6.70	14.33	26.61	32.38	42.41
2. Union Bank of India	April 1, 2020	-69.45	-25.08	-12.49	4.54	7.73	12.34
3. Punjab National Bank	April 1, 2020	-55.39	-30.94	0.62	2.08	3.16	2.28
4. Canara Bank	April 1, 2020	-70.47	4.71	-26.50	16.91	32.49	58.45
		31-03-2017	31-03-2018	31-03-2019	31-03-2020	31-03-2021	31-03-2022
5. Bank of Baroda	April 1, 2019	6	-10.53	1.64	1.36	1.78	14.06

		31-03-2015	31-03-2016	31-03-2017	31-03-2018	31-03-2019	31-03-2020
6. State Bank of India	April 1, 2017	17.55	12.98	13.43	-7.67	0.97	16.23

(Source: Annual Reports, Ministry of Corporate Affairs)

Table No. 4 shows that both Indian Bank and Canara Bank's EPS increased significantly following the merger. The EPS of Bank of Baroda, PNB, and Union Bank of India was negative prior to the merger, but it was positive following it. However, SBI's earnings per share (EPS) peaked at 17.55 prior to the merger, declined following the merger (-7.67), and then increased (0.97) in the next fiscal year, followed by a notable increase in the subsequent year.

Conclusion

In conclusion, this study on mergers and acquisitions (M&A) in the Indian banking sector highlights the significant role these strategies play in fostering sustainable economic growth, improving financial performance, and enhancing market competitiveness. The analysis of key financial metrics such as Return on Assets (ROA), Return on Equity (ROE), Net Profit Ratio, and Earnings Per Share (EPS) shows marked improvements for most banks following their mergers. This improvement can be attributed to several factors.

Firstly, the economies of scale and cost efficiency achieved through consolidation have allowed banks to reduce operational expenses by sharing infrastructure and administrative functions. This is evident in the enhanced profitability metrics for banks such as Indian Bank, Canara Bank, and Union Bank of India. Secondly, mergers have enabled risk diversification by expanding the asset base of the merged entities, thereby reducing exposure to specific sectors or regions. This diversification has helped stabilize the financial performance of banks like Punjab National Bank and Bank of Baroda, as demonstrated by their improved EPS and Net Profit Ratios.

Additionally, M&A activities have facilitated technological advancements and digital transformation within the banking sector. By merging with technologically advanced institutions, banks have been able to enhance their digital capabilities, leading to better customer retention and satisfaction, which in turn contributes to increased profitability post-merger. Moreover, mergers have strengthened the financial health of banks, enabling them to meet regulatory requirements more effectively. The infusion of capital during these mergers has provided much-needed financial stability, as seen in the case of banks like SBI and Canara Bank, despite SBI's temporary declines in certain metrics.

Overall, the findings underscore that mergers and acquisitions are not only critical for improving financial performance but are also essential for positioning Indian banks as globally competitive institutions. However, the success of these mergers is contingent on strategic alignment, effective integration, and the ability to overcome operational challenges. By fostering global expansion and synergy, mergers in the Indian banking sector have laid a strong foundation for future growth and economic development.

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