Volume: 1 Issue: SP14 Pages: 01-06

International Journal of Research in Academic World

E-ISSN: 2583-1615
Impact Factor: 4.714

Received: 02/September/2022 Int. J Res. Acad. World. 2022; 1(SP14):01-06 Accepted: 03/October/2022

Merger and Acquisition of Indian Bank: Boon or Curse for Indian Economy

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Abstract

Banking industry plays important role in money creation in economy, it accepts deposits from people and gives loans and advances. This study aims to analyze the effect of merger and acquisition of banks on Indian economy, whether it is beneficial or not. Taking advantage of economies of scale is one of the primary goals of banking mergers and acquisitions. This study is based on secondary data which is collected from related journals, websites and e-newspapers. This study found that through merger liquidity of banks can be increased which helps in boost the economy, risk can be diversified, ill performing banks can be survived, technology can be improved and can be confronted the issues of NPAs. With the help of help of merger banks will be able to compete, build a few strong banks which form a pillar of the economy, big banks can better deal with NPAs, create economies of scale in operation, investors' confidence increase and strong banks attracts investments. At the time of merger some problem also faced by banks such as, each banks laws and policies are different, the ramifications of a failure of a large bank are enough to devastate the country's economy, due to inefficient NPA policies and regulatory forbearance mergers will not alleviate the problem of nonperforming assets, there are issues with synchronisation and there is no guarantee that the newly established banks will be able to compete in the global market. It shows that merger of banks has both positive and negative impact on Indian economy. This study concluded that merger of banks has advantages as well as disadvantages, its two wheels of the same vehicle that move together.

Keywords: Indian banking, merger and acquisition, Indian economy

Introduction

A bank is a sort of financial entity that can receive deposits and lend money. Among the several sorts of banks are retail banks, commercial or corporate banks, and investment banks. In most countries, banks are regulated by the government or the central bank. Commercial banks assist the Indian government in attaining each goal of the country's planned economic development, hence the banking industry plays an important role in the Indian economy. The financial system is tremendously important in today's economy. Banks receive money from individuals and then lend it to entrepreneurs and manufacturers. The combining of two or more banks is known as a bank merger. A new bank is formed or the acquirer bank (buyer) bank is established when a bank merges with another bank and purchases its assets and ownership. In terms of acquisition, it's crucial. Bank mergers can be beneficial or harmful. Mergers help businesses by allowing them to combine their operations and initiatives. By working together, they can increase shareholder value and better meet customer needs. We may also argue that the merger facilitates the removal of restraints and the acquisition of a market-leading competitive advantage.

History of Bank in India

The "Bank of Hindustan," the country's first bank, was founded in 1770 in the then-Indian capital of Calcutta. This bank, on the other hand, did not prosper and eventually failed in 1832. Over 600 banks were registered in the country prior to independence, but only a few survived. During British administration in India, the East India Company established three banks known as the Presidential Banks: Bank of Bengal, Bank of Bombay, and Bank of Madras. In 1921, the three banks amalgamated to become the "Imperial Bank of India," which became a single entity. In 1955, the Imperial Bank of India was nationalized and renamed The State Bank of India, and it is now the largest public sector bank in India.

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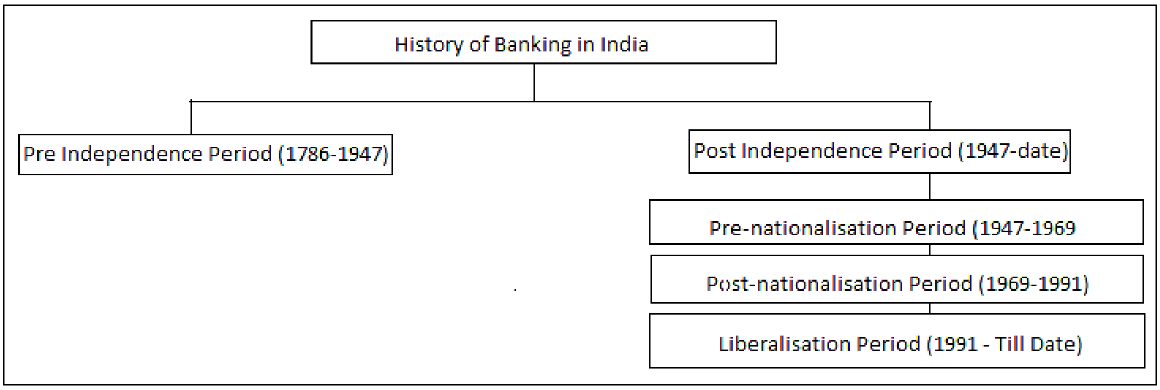

Fig 1: History of banking in India

Several banks were created prior to independence, including Allahabad Bank in 1865, Punjab National Bank in 1894, Bank of India in 1906, Central Bank of India in 1911, Canara Bank in 1906, and Bank of Baroda in 1908. Many big banks failed to exist in the pre-independence period due to a lack of machines and technology; Indian account holders had become vulnerable to fraud; there were fewer facilities; human errors were costly; and management skills were lacking.
Then post-independence era came which brought some good changes in Indian banking scenario, the post-independence era was from 1947 to 1991. The first thing happened after independence was government decided to nationalize banks so that rural people can also avail services of banks and get rid of money lenders. Banks were nationalized under the Banking Regulation Act, 1949 and Reserve Bank of India nationalized in 1949. After this State Bank of India was formed in 1955 and following this during 1969 to 1991 several banks were nationalized, in 1969 14 banks were nationalized whose national deposits were more than 50 cr. Namely, Allahabad Bank, Bank of India, Bank of Baroda, Bank of Maharashtra, Central Bank of India, Canara Bank, Dena Bank, Indian Overseas Bank, Indian Bank, Punjab National Bank, Syndicate Bank, Union Bank of India, United Bank and UCO Bank. In 1980 six more banks were nationalized namely Andhra Bank, Corporation Bank, New Bank of India, Oriental Bank of Commerce, Punjab & Sind Bank and Vijaya Bank. Apart from these 20 banks in 1959 seven subsidiary of SBI were also nationalize namely State Bank of Patiala, State Bank of Hyderabad, State Bank of Bikaner & Jaipur, State Bank of Mysore, State Bank of Travancore, State Bank of Saurashtra and State Bank of Indore. Later these banks merged in 2017 in SBI. In 1975 regional rural banks were established for expanding banks in rural areas.
We view the time following 1991 to be the liberalisation phase, the government decided to set up a committee led by Shri. M Narasimham to oversee the numerous reforms in the Indian banking system in order to bring stability and profitability to the Nationalised Public Sector Banks. In this era privatization of banks were biggest development, The Reserve Bank of India has approved the establishment of ten private sector banks in the country. The following banks were among them: Global Trust Bank, ICICI Bank, HDFC Bank, Axis Bank, Bank of Punjab, IndusInd Bank, Centurion Bank, IDBI Bank, Times Bank and Development Credit Bank. Some other steps were also taken such as, set up branches of foreign banks in India, the committee declared that the RBI and the government would treat public and private banks equally. Payments banks were created with the progress in the field of banking and technology, and any foreign bank might start joint ventures with Indian banks, small finance banks were given permission to open branches all over India, with internet banking and apps for financial transfers and a large portion of Indian banking has shifted online.
An acquisition is when one firm buys another outright. A merger is the coming together of two businesses to form a new legal entity under a single corporate name. A merger is described as "a merger of two or more corporations in which the selling firm(s) assets and liabilities are absorbed by the buying firm." The buying firm preserves its original name, despite the fact that it may be a quite different organisation following the merger." "An acquisition," on the other hand, is when one firm buys the majority or all of the shares of another company in order to obtain control of it. Buying more than half of a target firm's stock and other assets permits the acquirer to make decisions about the newly acquired assets without the company's shareholders' consent.

Review of Literature

Vansh Ved (2021) [6] this study conclude that a good merger can increase an industry's economics as well as the market in ways that nothing else can. Employment, R&D, improved capital flow, greater shareholder returns, and limitless expansion opportunities Mergers and acquisitions have proven to be a boon to small businesses striving to stay afloat without selling out to larger corporations with deep coffers. A merger allows a company to raise additional funds, which improves its long-term viability. Overall, the benefits of a merger to the Indian economy significantly outweigh the disadvantages in the long run.
Sharma Deeksha (2020) [1] this paper has reviewed literature on merger and acquisition of banks in India. This study has conducted to know positive and negative impact after merger and acquisition of banks, also causes behind merger and acquisition of bank has been studied. Secondary data was used for this study, this study concluded that positive effects have been seen on merged bank.
Ishwarya J (2019) [2] this paper looked at merger and acquisition of Indian banking and studied long term implications of the mergers, also analysed emerging trends and recommended steps that bank should consider for future. This paper reviewed the trends in merger and acquisition in Indian banking and their impact also studied. This paper compared pre and post-merger financial performance of merged banks with the help of financial parameters. Secondary data were collected for the study. The findings of the study suggested that to some extent merger and acquisition has been successful but government and policy makers should not promote merger between strong and distressed banks, because it has adverse effect upon the asset quality of the stronger banks. This paper also studied the SBI

and its associate's merger with their pros and cons of the banks.

Indrapriya S. (2018) [3] this paper dealt with the mergers and acquisitions, types of mergers, legal framework, approval of Reserve Bank of India and historical perspectives of banks M& A, impact of mergers and acquisition in banking industry. This study aims to know about the merger between HDFC and Centurion Bank if Punjab. This study is descriptive in nature so secondary data was used for this study. This study concluded that the concept of merger and acquisition can also be a risky process which has to be adopted, as it may bring various problems to the company in terms of the management, it working, etc.

Dr Ravi B (2019) [4] According to this, the involvement of the central government in the entire process of merger and amalgamation must also be examined, as they play a critical role in policy formation necessary for the expansion of Indian banking. They looked at the Bank of Madura's merger with ICICI Bank, ICICI's reverse merger with ICICI Bank, Centurion Bank and Bank of Punjab merging to form Centurion Bank of Punjab, and Lord Krishna Bank's latest decision to join with Federal Bank as voluntary initiatives by banks to consolidate and grow. The study suggests that in a changing economic and commercial climate characterised by speed, flexibility, and consumer response, scale plays an important role in staying competitive. In this setting, mergers and acquisitions (M&As) as an instrument for gaining competitive power emerge, with partnering for competitiveness as a recognised strategic argument for the same.

Meena S, kumar P (2014) [5]. This research paper looked at Mergers and Acquisitions (M&A's) that have happened in Indian banking sector to understand the resulting synergies and the long-term implications of the merger. This paper reviewed the trends in M&A's in Indian banking and then impact of M&A's has been studied in three leading banks of India. This study covered the area of performance evaluation of M&A's in Indian banking sector during the period from 2000 to 2013 and also compared pre and post-merger financial performance of merged banks with the help of financial parameters like, Net Profit margin, operating Profit margin, Return on Capital Employed, Return on Equity, earnings per share, capital adequacy ratio, dividend per share etc. The findings suggested that to some extent M&A's has been successful in Indian banking sector. The Government and Policy makers should not promote merger between strong and distressed banks as a way to promote the interest of the depositors of distressed banks, as it will have adverse effect upon the asset quality of the stronger banks.

Statement of the Problem

What is the impact of merger and acquisition of banks on Indian economy and why merger and acquisition needed?

Objective of Study

1. To learn about the reasons behind bank mergers and acquisitions in India.
2. To understand the benefits and drawbacks of bank mergers and acquisitions on the Indian economy.

Research Methodology

This study is descriptive in nature, Secondary data on impact of mergers and acquisitions in the Indian banking sector on economy is acquired from various research papers, websites, and e-newspapers.

Need for the Study

Deregulation and liberalisation, as well as divestment of public sector banks, entry of foreign banks, and mergers of many banks in India and around the world, have significantly transformed the banking sector's structure since the early 1990s. About 25 bank mergers occurred in India following the reforms. This study focuses on the influence of mergers and acquisitions on the Indian economy because M&A's of banks have such a large impact on the Indian economy.

Causes of Merger and Acquisition in Indian Banks: After analysing several previous studies following are the reason because of which merger and acquisition happens in Indian banking system:

1. **Merger of Banks with a Lower Capital Base:** The practise of merging weaker banks with bigger banks was advocated in order to offer stability to weaker banks, however the Narasimhan committee disagreed. Mergers, they claimed, can help diversify risk management.
2. **Market Competition is Increasing:** Mergers are motivated by the development of new financial products and the consolidation of regional financial systems. Markets became increasingly competitive as they became more industrialised, and as a result, all individual enterprises' market share dropped, prompting the start of mergers and acquisitions.
3. **Economies of Scale:** When a large number of people work on something at the same time, this is known as a scale economy. When businesses join together, they can benefit from economies of scale.
4. **Talent & Skill:** A skill allocation occurs between two organisations, allowing them to improve and become more competitive.
5. **Products and Technology:** E-banking and some monetary instruments/derivatives are introduced. Because the admittance barrier was removed, new banks with advanced technology were able to enter the market, and existing banks were unable to compete, thus they decided to merge.
6. **Advantageous Synergies:** When two companies merge, their main goal is to produce a positive outcome that is greater than the combined effect of the two organisations working separately. It has two features: cost synergy and revenue synergy.
7. **Survival of Poor Banks:** Banks with poor performance survived mergers and had their branch network geologically expanded.
8. **Larger Customer Base:** with the help of merger banks can reach to more customer even to rural people also which increase market share.
9. **Enhanced Technology:** To compete with international banks in a global era, banks must build infrastructure, limit competition, reduce bank congestion, and exploit underutilised resources.

Provisions Relating to Merger and Amalgamation of Banks

Mergers-Banking Regulation Act, 1949

- Section 44A of this act talks about the procedures for voluntary mergers of banking companies.
- Section 45 of this act talks about the compulsory amalgamation of banks.

Companies Act 2013

- Selection 230 and 232 of the Companies Act, 2013 relates with the mergers and amalgamation.

State Bank of India, 1955

- Section 35states acquisition of business of other banks by State Bank of India.

Bank Merger List in India 2021

The government of India (GoI) has merged 10 public sector banks into four new institutions. Union Finance Minister Nirmala Sitharaman made the announcement of this mega-merger in 2019. Following table shows the recent merger happens in banking industry in past few years.

Table 1: List of merged banks

Acquiring bank	Amalgamated bank	Acquisition date
Indian Bank	Allahabad Bank	1-Apr-20
Punjab National Bank	Oriental Bank of Commerce	1-Apr-20
Punjab National Bank	United Bank	1-Apr-20
Union Bank of India	Andhra Bank	1-Apr-20
Union Bank of India	Corporation Bank	1-Apr-20
Canara Bank	Syndicate Bank	1-Apr-20
Bank of Baroda	Vijaya Bank, Dena Bank	1-Apr-19
State Bank of India	State Bank of Bikaner & Jaipur	31-Mar-17
State Bank of India	State Bank of Hyderabad	31-Mar-17
State Bank of India	State Bank of Mysore	31-Mar-17
State Bank of India	State Bank of Patiala	31-Mar-17
State Bank of India	State Bank of Travancore	31-Mar-17
State Bank of India	Bharatiya Mahila Bank	31-Mar-17

Above table no. 1 shows the acquiring bank and amalgamated with the date of their merger.

Current Status of Indian Banking Industry: Currently according to RBI report, in addition to cooperative credit institutions, India's banking system includes 12 public sector banks, 22 private sector banks, 44 foreign banks, 43 regional rural banks, 1,484 urban cooperative banks, and 96,000 rural cooperative banks.

Impact of Merger and Acquisition on Indian Economy

Because the banking sector is the foundation of our economy, it is critical to keep it healthy and strong. The Reserve Bank of India (RBI), which governs the banking sector of the Indian economy, keeps a close eye on how banks operate in the country and develops rules and regulations based on current economic, international, social, and other variables. The fact that our banking system is beset by nonperforming assets (NPAs) is well known, and the situation is deteriorating by the day. Wilful defaults, frauds, and the failure of business houses have resulted in this circumstance. With each passing day, the problem of nonperforming assets (NPAs) becomes more serious. This ordeal has worsened as a result of the issues listed above, but it is important to note that bank mismanagement and inefficiency have also played a role in exacerbating the problem. All of these elements, together with the goal of improving the banking sector, were seen to be causing a paradigm shift in the banking industry, which would not only offer a boost but also curb the sector's flaws.

Every decision made by the government is for the betterment of the system and to increase its robustness, but it cannot be denied that it may have flaws that cannot be anticipated at the time the decisions are made, or the negative impact that those decisions may have when they are implemented at the grassroots level. As a result of this issue, the government implements regular policy adjustments in order to strengthen the system. Considering the foregoing, this enormous merger activity in the banking sector will have both beneficial and bad consequences, which will be evident as time passes. But, as far as can be observed at this point, it will have a positive impact on our economy.

Positive Impact of Merger and Acquisition on Indian Economy

1. **Reducing the NPAs:** Bad loans and nonperforming assets (NPAs) are one of our banking system's most serious issues, impeding overall economic growth. NPAs have been rising at an alarming rate, putting the country's financial system in jeopardy. The government has made an attempt to ensure that substantially weaker banks are not pushed out of the market due to poor loans/NPAs by merging them with stronger banks.
2. **The Legal Cost and Other Ancillary Costs will Comparatively Come Down:** The same borrower has taken out loans from multiple banks, as can be observed. They spend a lot of money every year on bad loan recovery; by lowering these costs, banks may save a lot of money. There have also been reports of squandering funds. With the merger of banks this cost come down.
3. **Good Financial Performance:** By merging banks, the banks will become bigger and better, as they will be able to serve a wider range of consumers than they already do. Customers will be able to get services through a single bank rather than having to go to multiple banks. Because the merged bank will benefit from synergies, having a large client base will help the banks to be profitable.
4. **A Stronger Position to Compete:** The amalgamated banks' business portfolios, asset quality, market capitalization, risk appetite, and risk management techniques will all be superior. There will be a very small probability of the banks failing. Following the merger, public banks will be better positioned to compete with private companies in the market.
5. **Economies of Scale:** The combined banks will benefit from economies of scale and lower operating costs. Following the merger, banks will be in a stronger position to finance large projects that they previously couldn't fund on their own, making the funding process for those projects faster and easier.
6. **Capable of Playing a Key Role in the International Banking System:** Indian banks have unable to establish a global presence after so many years. There are various causes for this, including the size of the balance sheet, operational insufficiency, failure to fulfil international banking norms, and so on. Not only will the banks have a global footprint after the merger, but they will also be able to play a key role in the international banking system.
7. **International Presence:** Prior to mergers, RBI had to manage a disproportionately high number of banks, making it a difficult responsibility. With fewer institutions to manage, the RBI will be able to impose the banking norms used in industrialised countries, bringing Indian banks up to level with banks with international operations. The State Bank of India is currently ranked among the top 50 banks in the world.
8. **A Considerable Reduction in Operational Costs:** The

post-merger era will drastically reduce operational costs. Banks will be able to reduce their overheads by saving money on treasury operations, audits, controls, technology, and management. Banks will be able to combine their resources and use them more effectively and efficiently as a result of the merger. The mergers will result in the rationalisation of branches, as well as the reduction of responsibilities and functions.

9. Bank consolidation will result in the formation of a few strong banks that will serve as a pillar of the economy.
10. Small banks and NBFCs are not in a position to lend more loans as the banking sector becomes increasingly stressed as a result of nonperforming assets (NPAs). Big banks may not have to stop making loans after the merger since they can better deal with non-performing assets.
11. Monetarists believe that bank mergers will be highly beneficial in the long run. Investor trust in strong banks is expected to be stronger than that in weak banks in terms of investment flows. Medium and small banks are currently dealing with a lack of investment. Strong banks have the resources to attract capital.

Negative Impact of Merger and Acquisition on Indian Economy

1. **Internal Clashes:** Internal conflicts and disagreements about promotions and other possible concerns may occur. Conflicts arise because different banks have distinct ideas and people with different backgrounds. People are concerned that they may lose their employment, despite the fact that their fears have been dispelled by the respected Finance Minister.
2. **The Technological Implementation will be Difficult:** Merger will undoubtedly yield numerous benefits, but technical implementation will be a time-consuming undertaking in and of itself. Because separate banks employ different software platforms, integrating them with the amalgamated bank will be difficult. Financial consolidation, as well as other financial issues, will need to be considered.
3. **Bank becomes Oversized:** It is stated that as a bank grows larger, it gets more difficult to oversee its operations, and that if the bank begins to fail, the entire economy is imperilled. Despite the fact that we are all familiar with the slogan "TOO BIG TO FAIL," any large bank or financial institution that collapses will have a negative impact on the whole economy.
4. **Reroute a Large Chunk of Management:** In the short term, consolidation of PSBs (public sector banks) may not only distract a major percentage of management and employee bandwidth away from expansion, but it also has the potential to stifle credit growth, halt recoveries, and hand market share to private banks. Following the merger of its associate banks, State Bank of India reported a substantial decline in loan off take. Following the merger of SBI and its associates, SBI management stated that credit and lending monitoring had taken a back seat since a major portion of its staff's efforts had been focused in the merger process. The benefits of the mammoth merger of these ten public sector banks are evident, but they will only last two to three years.
5. **Loan Growth has Slowed:** Experts believe that, despite the government's allocation of additional capital and drive for co-lending, loan growth would decrease, as seen in previous mergers, which cannot be beneficial at a time when liquidity flow is severely constricted.
6. The ramifications of a failure of a large bank are enough to devastate a country's economy, making it a dangerous idea.
7. While the fundamental purpose of bank mergers appears to be the ever-increasing problem of non-performing assets, mergers may not be the solution.
8. Synergy proves to be a critical component of any successful merger. However, there will be synchronisation issues in the current environment.
9. Banking is still not well-integrated into Indian saving habits. Regional banks built a level of trust in the public that will be lost as a result of mergers.
10. Customers are frequently affected by mergers in an emotional way. It is possible that if customer impression is not managed sensitively, it will result in a loss of business.

Conclusion

The government has taken several efforts for the welfare of the country at regular intervals. Some of these produce benefits right once, while others take time to show results. The outcome of this gigantic merger is debatable, and the merger's fate will be decided in the future. The political, economic, social, and technological architecture all have a role in whether or not mergers have the potential to have a good influence. In India, the actions taken in relation to bank mergers are taken with the best of intentions. It is up to you to decide whether the benefits exceed the drawbacks. Both advantage and disadvantages go together, merger of banks have both impact positive and negative on Indian economy. Positive and negative impact of merger on economy is two side of the same coin. Advantages of banks merger includes economic growth, expansion of market share, tax benefit, entry in global market and better management of banking capital. And limitations include Very challenging to manage the people and culture of different bank, Risk of public debt, Governance issues and Chances of Bank going Bankrupt. This study conclude that mergers are important for Indian economy for the expansion purpose and for economic growth purpose still it have some disadvantages which can be ignore with proper management of banks administration.

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