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A Study on Merger and Acquisition of Banks and a Case Study on STATE BANK OF INDIA and BANK OF SAURASTHRA

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Abstract

This research paper is an attempt to study Merger and Acquisitions (M&A's) that occurred in Indian banking with reference to SBI and BANK OF SAURASTHRA to understand the outcomes and the long term merits and demerits of the merger. The study covers the area of financial performance of key indicators after M&A's in both these banks during the pre and post period of merger. The paper attempts to compare financial indicators performance pre and post merger of these two merged banks with the help of different financial ratios and evaluating their parameters. It also studies the State Bank of India and Bank of Saurasthra with the pros and cons of the financial parameters for banks. The required data are collected from secondary source.

Keywords: Merger, Acquisitions, State bank of India and it associates

INTRODUCTION

The banking system in India has gained outstanding achievements, in a comparatively short time, for the World's largest and the most diversified democracy. There have been several reforms in the Indian banking sector, as well as quite a few successful merger and acquisitions, which have helped it, grow.

In the year of 1968 the Government of India issued an ordinance by which 14 large commercial banks in the country were meant to be nationalized. These fourteen banks, at that time comprised of whooping eighty five per cent of the total bank deposits in our country. In the year 1980, another round of nationalization happened and six more commercial banks came under the flag of government control. With this step government begun to enjoy ninety one per cent of the banking sector under their direct control and the number of nationalized banks in country went up to sum 20 in number. Once again in the year **1993**, Indian government took yet another step towards economic reforms to achieve economical heights and made a turn towards merger of banks. The New Bank of India was merged with the Punjab National Bank (PNB). This was the first merger between nationalized banks, ever happened in Indian history and due to this, the number of nationalized banks in India were reduced from twenty to nineteen.

In today's global marketplace, banking organizations have greatly expanded the scope and complexity of their activities and face an ever changing and increasingly complex regulatory environment.

Explaining the concept and Meaning of Merger

A merger is defined as a deal to combine two existing companies into one new company. There are several types of merger and also several reasons for companies to merger. Most merger amalgamates two existing companies into one newly named company. Merger and acquisitions are commonly done to expand a company's reach, expand into new verticals or to increase market share**.**

Explaining the concept and Meaning of Acquisition

An acquisition is defined as a corporate action in which a company buys most of another firm's ownership stakes to assume control of it. An acquisition occur when a buying company obtains more than 50% ownership in a target company. As part of the exchange, the acquiring company often purchases the target company's stock and other assets, which allows the acquiring company to make decisions regarding the newly acquired assets without the approval of the target company's shareholders.

LITERATUREREVIEW

Several studies have been conducted to examine the impact of merger and Acquisition.

In a study conducted by Anand Manoj & Singh Jagandeep (2008) the impact of merger announcements of five banks on the share holder part in the Indian Banking was studied.

The declaration of merger of Bank had positive impact on share holder's wealth. There was a positive effect on both the acquiring and the acquired banks.

In an another study by Sinha Pankaj & Gupta Sushant (2011), pre and post analysis of firms was studied and conclusion withdrawn was that there was a positive effect as their profitability, in almost cases deteriorated liquidity. After few year of Merger and Acquisitions(M&As) it came in to light that companies may have been able to balance the outcomes arising out of the merger and Acquisition that failed to manage their liquidity

OBJECTIVES OF THE STUDY

The objectives of the study are as follows:

1. To study Post Merger and Acquisition influence on profitability standards of the surviving company.
2. To analyse Post Merger and Acquisition effect on leverage standards of the surviving company.
3. To determine Post Merger and Acquisition liquidity position of the surviving firm.
4. To ascertain Post Merger and Acquisition improvement in capital market standards of the surviving company.

NATURE OF DATA AND SOURCES OF DATA

Collection of the data is essential part of research. The nature of data which is collected and used for this research is secondary in nature. The relevant and required data has been collected from journals, annual reports, magazines, and websites of selected companies and through various search engines (Google, Yahoo, Bing etc.). Due to unavailability of old data of companies the data has been collected from various research journals, archives of financial websites. Available annual report's data have been taken into account from archive of Dion Global Solutions Pvt. Ltd.

SAMPLE SELECTION

STATE BANK OF INDIA (ACQUIRER) AND BANK OF SAURASTHRA (TARGET)
The Date of Merger: 13 August 2008.
Data taken in study from period 2005-2008 in pre-merger and 2010-2014 for post-merger.

RESEARCH HYPOTHESES

In order to achieve the objectives of the study, the following hypothesis are framed:

H_0 Post-Merger and Acquisition, there was no significant improvement observed in profitability standards of the Acquiring companies.

H_a Post-Merger and Acquisition, there was significant improvement observed in profitability standards of the Acquiring companies.

H_0 Post-Merger and Acquisition, there was no significant improvement observed in leverage standards of the Acquiring companies.

H_b Post-Merger and Acquisition, there was significant improvement observed in leverage standards of the Acquiring companies.

H_0 Post-Merger and Acquisition, there was no significant improvement observed in liquidity position of the Acquiring firm.

H_c Post-Merger and Acquisition, there was significant improvement observed in liquidity position of the Acquiring firm.

RESEARCH METHODOLOGY

To test the effect of the merger happened we scrutinized on the performance various ratios including net profit ratio, return on total assets, return on shareholder's equity, EPS, Net worth of share and certain liquidity ratios were calculated from the collected financial and accounting data, for five year pre-merger and five year Post merger. Keeping in view the objective of the study, Independent Two tailed t-test was employed on individual ratios. This has been used as a statistical tool to find out whether the merger had any significant effect on a given ratio or not.

DATA ANALYSIS

Consolidation of business entities is a world-wide phenomenon. One of the tools for consolidation is merger and acquisitions. In order to analyze the data descriptive statistics are used in addition to two tailed t-test. The t-test has been applied on the different ratios of pre and post merger to look upon the effect on standards of profitability, liquidity, leverage, capital market structure. Pre and post- merger performance ratios have been calculated for the entire set of sample, which have gone through Merger and Acquisition during the selected period. The pre and Post-Merger and Acquisition performance ratios have been compared to check the performance of acquirer firm after merger and acquisitions, statistical tool "paired sample t-test" is used. The confidence level of 0.01 or 99% level of confidence was computed along with descriptive statistics.

Data analysis and Interpretation

Pre and post- merger performance ratios have been calculated for selected banks for the pre and post-merger and acquisition performance ratios have been compared to see if there is any statistically significant change in performance of acquirer firm after merger and acquisitions, using "paired sample t-test" at confidence level of 0.01 or 99% level of confidence along with descriptive statistics.

SBI AND BANK OF SAURASTHRA

Central Board of State Bank of India granted its permission for the merger of State Bank of Saurashtra on 25 August 2007. As Merger needed the mandatory approval from the government of India and Reserve Bank of India as predefined with State Bank of India Act, 1955. For its shake SBI wrote a letter to Mumbai Stock Exchange, that its central board on August 25 has approved and SBI is ready for the merger of bank of Saurasthra, conditioned to approval from government of India and Reserve Bank according to the defined State Bank of India Act, 1955.

State Bank of Saurashtra at that time of merger had 460 branches across the country so its merger would help removal of twin branches in the same area. The net profit of bank went up to INR 87.4 crore in the year 2006-07. With a paid-up equity capital of 314 crore INR and total deposits 15,804 INR crore while total advances showed in books were INR 11,081 crore.

The merger was thought to help SBI consolidated and enjoy its position of the country's biggest bank and legg nearest rival ICICI Bank way behind. With a total of 9,579 branches across the globe SBI had total assets of INR 5,66,565 crore and a net profit of INR 4,541 crore.
The merger happened at the time when the bank already had decided for its expansion. The bank also looked at that time freeing up capital by setting up a holding company for its life insurance and asset management businesses. SBI’s move to merge its arms could pave the way for further consolidation in the industry.

t-test table of financial ratios for State Bank of India and State Bank of Saurashtra

LEVERAGE	Arithmetic Mean pre-merger	Arithmetic Mean post-merger	Standard deviation(pre)	Standard deviation(post)	t-value	Significance (2-tailed)
Interest coverage ratio	15.55	14.382	1.57	1.22	178	0.901
Debt-equity ratios	15.36	13.16	1.55	1.13	165	0.873
LIQUIDITY						
Current ratios	0.046	0.05	0.012	0.007	1.581	0.153
Acid ratio	5.60	6.98	0.658	2.26	-5.099	0.005
CAPITAL MARKET STANDARDS						
EPS	83.93	131.53	26.14	34.21	-2.959	0.018
PROFITABILITY						
ROA	16.62	14.45	2.19	2.19	2.406	0.043
ROE	15.93	16.55	1.64	2.19	2.189	0.012
Net profit ratio	10.96	11.40	0.728	1.63	2.84	0.022

Data analysed in above table concludes that ROE return on equity ratio, ROA return on assets, EPS earning per share, acid ratio and net profit ratio has the significance below 0.05 that means profitability standard along with liquidity and capital market standards has some effect and leverage standard is not affected for the tested period of data. Hence it can be said that hypothesis 1, 3 and 4 are accepted and hypothesis 2 is rejected and the alternate is accepted.

Which are as given below:

1. Post-Merger and Acquisition, significant improvement was shown in profitability standards of the State Bank of India.
2. Post-Merger and Acquisition, no significant improvement was shown in leverage standards of the State Bank of India..
3. Post-Merger and Acquisition, significant improvement was shown in liquidity position of the State Bank of India..
4. Post-Merger and Acquisition, significant improvement was shown in capital market standards of the State Bank of India..

It shows that there is a change in profitability, liquidity and capital market standards of surviving company.

The merger of STATE BANK OF INDIA and STATE BANK OF SAURASTHRA is taken in account under the light of financial ratios which draws the conclusion.

1. For Debt equity ratio the average mean pre-merger is calculated 14.36 and post-merger the mean is 14.22 hence the indicator showed a good performance in terms of financing.
2. For Current ratio the average mean pre-merger is calculated 0.50 and post-merger the mean is 0.40 hence the liquidity showed the loss and the performance is not good.
3. For Acid ratio the average mean pre-merger is calculated 5.74 and post-merger the mean is 11.13 which shows good performance in terms of covering immediate liabilities by short-term assets.
4. Calculating EPS the average mean pre-merger is 100.40 and post-merger is 157.39 that show the earning per share had an increment and is a far better indicator in terms of merger for State bank of India.
5. For return on assets the mean average pre-merger is 15.86 and post- merger is 12.52 which is not a good performance indicator post-merger for State bank of India.
6. For return on equity the mean average pre-merger is 16.53 and mean average on post-merger is 13.85 that also is a bad indicator for State bank of India.
7. Calculating Net profit ratio mean average is 11.31 to 9.04 post-merger. This indicated a sign of loss the result of merger for State bank of India.

S.No	Ratios	Performance
1	Debt equity ratio	Good
2	Current ratio	Poor
3	Acid ratio	Good
4	EPS	Good
5	ROA	Poor
6	ROE	Poor
7	Net profit ratio	Poor

The merger of State bank of India with State bank of Saurasthra has mixed results in terms of financial gains as shown by financial ratios above.

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