International Journal of Trend in Scientific Research and Development (IJTSRD)
Volume 5 Issue 2, January-February 2021 Available Online: www.ijtsrd.com e-ISSN: 2456 – 6470

Mergers and Acquisitions in Indian Banking Sector (A Case of Bharat Overseas Bank and Indian Overseas Bank)

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ABSTRACT

Mergers and Acquisitions (M&As) continue to be a significant force in the restructuring of the financial services industry. The Indian Commercial Banking Sector, which has played a pivotal role in the country's economic development, is currently passing through an exciting and challenging phase. The present research papers studies the impact of M&A on the financial performance of Bharat Overseas Bank and Indian Overseas Bank. The study uses key financial ratios to find the impact of M&A on financial performance of selected banks.

KEYWORDS: *M&As, Restructuring, Bank, financial Ratios*

How to cite this paper: Dr. Soniya Gambhir "Mergers and Acquisitions in Indian Banking Sector (A Case of Bharat Overseas Bank and Indian Overseas Bank)" Published in International Journal of Trend in Scientific Research and Development (ijtsrd), ISSN: 2456-6470, Volume-5 | Issue-2, February 2021, pp.372-375, URL: www.ijtsrd.com/papers/ijtsrd38415.pdf

IJTSRD38415

INTRODUCTION

The economy of India is tending to spread very quickly and has been emerging at the highest place whether it be Information technology, Research and development, pharmaceutical, infrastructure, energy, consumer retail, telecom, banking, Financial services, media and hospitality etc. The banking sector of India is examined to be the biggest growing sector and the soundness of the banking system has been extremely important for the development of the country's economy. To meet this changing scenario the bank can adopt the plan of action like Mergers and Acquisitions (M&As).

MEANING OF MERGER AND ACQUISITIONS (M&As)

Golbe and White (1993)[1] were among the first to observe the cyclical pattern of Merger and Acquisitions (M&As) activity.

Through mergers and acquisitions, a company can develop a competitive advantage and ultimately increase shareholder value. **Kithinji and Waweru (2007)**[2] describe merger as a process in which one of the two companies loses its identity to make a one firm.

Pandey (2011)[3], states A merger is said to occur when two or more companies combine into one company. **Pandey (2011)**[3], defines" Acquisition may be defined as an act of acquiring effective control over assets or management of a company by another company without any combination of business or companies".

Types of Mergers:

From the view point of an economist i.e. based on the relationship between the two merging companies, mergers can be classified as follows:

1. **Horizontal Merger:** According to **Khan and Jain (2014)**[4], Horizontal merger is a Merger two or more firms dealing in similar lines of activity combine together.
2. **Vertical Merger**: According to **Khan and Jain (2014)**[4], Vertical merger is that merger that involves two or more stages of production/distribution that are usually separate.
3. **Conglomerate Merger:** According to **Khan and Jain (2014)**[4], Conglomerate merger is a merger in which firms engaged in different unrelated activities combine together.

M&A always comes with risk, especially in a changing landscape, the greater risk may be failing to partner to navigate uncertainty and add financial strength and operational resiliency.[5]

The concept of merger can be defined as " A combination of two or more companies in which the assets and liabilities of the selling firms are absorbed by the buying firm.[6]

M&As in the banking sector have been on the rise in the recent past, both globally and in India. The International banking scenario has shown major turmoil in the past few years in terms of mergers and acquisitions. Deregulation has been the main driver, through three major routes: dismantling of interest rate controls, removal of barriers between banks and other financial intermediaries, and lowering of entry barriers.

The Success of these M&A's depends on to a large extent upon a banks ability to assess the relatedness of the assets of both banks and the cultural differences as well as to being able to integrate and the cultural differences as well as to able to integrate the two banks"[7]

Merger of Bharat Overseas Bank (BOB) and Indian Overseas Bank (IOB)

Bharat Overseas Bank was established in the year 1973. It was a private sector bank based in Chennai. In the year 2007, BOB was merged with IOB. IOB tool over all employees, assets and deposit of BOB. The bank with a network of 103 branches was taken over by Indian Overseas Bank on March 3, 2007.

REVIEW OF LITERATURE

Most of the mergers are actually acquisitions in banking sector. An organization or a business actually buys another business and integrate it into its own business representation

Bansal and Kumar (2008)[8], evaluates that while moving towards mergers and acquisitions, the management of the company smells financial strategy and operating strategy in different ways. The study focuses on finding out that when the firm goes for M&A activity, the claims made by the corporate sector are being achieved or not in Indian context. For the purpose of analysis secondary financial data of various firms has been taken. Ratio analysis, correlation has been used for analysis.

Jalandhar, et al. (2011)[9], examined the performance evaluation of Indian Commercial Banks in terms of growth in Profitability, Revenues, Investment, Deposits and Total Assets. Bank mergers do not mean merging of two Balance sheets. After merger the biggest challenge for the banks is to manage employees and customer relationships. The researcher further concluded that the real benefits of merger is derived from development in technology, the need to maintain economic capital in relation to the risks a bank is exposed to, and the imperative of confronting to best international practices and standards in risk management.

Sinha P. and Gupta S. (2011)[10], analyses the data for of eighty cases M&A from 1993-2010. The study indicates that Profit after tax and Profit before Depreciation, Interest and Tax have positively changed after the merger but the liquidity position which is represented by Current Ratio has declined. After Merger it came to find that companies may have been able to leverage the synergies arising out of merger and Acquisition that have not been able to manage their liquidity.

Deverajjappa (2012)[11], explores the various reasons for merger in Indian Banking sector. The study is based on pre and post merger financial performance of Indian banks by analyzing various financial parameters like Gross profit margin, Net profit margin, operating profit margin, Return on capital employed, Return on equity, Debt equity ratio. The study uses Independent T-test to find significance level. The result concluded that after merger the financial performance have been increased.

Kouser and Saba (2012)[12], in the study examines the CAMEL model. The paper states that CAMEL is a suitable and simple model for evaluating the financial and managerial performance of banks. The paper evaluates that CAMEL is the most commonly used model for the assessment of performance and ranking. The ratios based on CAMEL model were analyzed using ANOVA to find out the significant difference between pre and post merger period.

Objectives of the Study

The present study is proposed to evaluate the financial performance of Bharat Overseas Bank and Indian Overseas Bank before and after the merger.

Hypothesis of the study

Ho = There would be no significant effect of Mergers and Acquisition on financial performance on selected Banks.

H1 = There would be significant effect of Mergers and Acquisition on financial performance on selected banks.

Data and Methodology

For the purpose of evaluating the financial performance before and after Merger and Acquisition a case of Bharat Overseas Bank and Indian Overseas Bank is selected through judgment as sample case.

The empirical study analyses the financial data of the merged banks before and after the merger. Since the merger took place in 31/03/2007 so, the financial analysis has been done for the year 2002 to 2006 (pre-merger) and from 2007 to 2012 (post-merger). The analysis has been done on the basis of key financial ratios using t-test. The data has been collected from secondary source using CAPITAL LINE database

Bharat Overseas Bank & Indian Overseas Bank

Analysis & Interpretation of Bharat Overseas Bank based on T-Test

The Descriptive **table 1** displays the sample size, mean, standard deviation, and standard error for both Pre and Post-Merger banks. On average after merger, the capital adequacy ratio of Bharat overseas bank decreased by 1.27%, total advance to total asset increased by 11.76%, Credit deposit ratio increased by 17.79%, Investment Deposit Ratio decreased by 2.44%, Cash deposit Ratio increased by 2.48%, Dividend payout ratio is increased by 9.41%, Return on Assets is increased by 0.08%, Return on Equity is increased by 4.25%,

Table1: Group Statistics of Bharat Overseas Bank

Group Statistics					
Pre-Post-Merger		N	Mean	Std. Deviation	Std. Error Mean
Capital Adequacy Ratio	Pre-Merger	5	14.1660	1.85284	.82862
	Post-Merger	6	12.8983	.89602	.36580
Total Adv. to Total Asset Ratio	Pre-Merger	5	49.1220	4.61344	2.06319
	Post-Merger	6	60.8750	2.45862	1.00373
	Post-Merger	6	73.6723	3.90562	1.59446
Credit Deposit Ratio (%)	Pre-Merger	5	55.1600	5.12518	2.29205
	Post-Merger	6	72.9483	3.31435	1.35308
Investment ratio (%)	Pre-Merger	5	35.9620	2.14260	.95820
	Post-Merger	6	33.5250	1.45352	.59340
Cash Deposit Ratio (%)	Pre-Merger	5	4.7400	.39799	.17799
	Post-Merger	6	7.2150	1.12269	.45834
	Post-Merger	6	.0417	.00753	.00307
Divident Payout ratio	Pre-Merger	5	15.0100	11.59527	5.18556
	Post-Merger	6	24.4150	8.31206	3.39338
Return on Assets (%)	Pre-Merger	5	.8540	.46317	.20714
	Post-Merger	6	.9317	.38881	.15873
Return on equity (%)	Pre-Merger	5	15.6160	8.57763	3.83603
	Post-Merger	6	19.8583	8.33152	3.40133

Analysis & Interpretation of Indian Overseas Bank based on T-Test

The Descriptive **table 2** displays the sample size, mean, standard deviation, and standard error for both Pre and Post-Merger banks. On average after merger, the capital adequacy ratio of Indian overseas bank increased by 0.52%, total advance to total asset increased by 9.08%, Credit deposit ratio increased by 20.96%, Investment Deposit Ratio decreased by 12.44%, Cash deposit Ratio decreased by 1.06%, Dividend payout ratio is increased by 4.075%, Return on Assets is decreased by 0.13, Return on Equity is decreased by 10.84.

Table 2: Group Statistics of Indian Overseas Bank

Group Statistics					
Pre-Post-Merger		N	Mean	Std. Deviation	Std. Error Mean
Capital Adequacy Ratio	Pre-Merger	5	12.3720	1.35981	.60812
	Post-Merger	6	12.8983	.89602	.36580
Total Adv. to Total Asset Ratio	Pre-Merger	5	51.7920	10.09089	4.51278
	Post-Merger	6	60.8750	2.45862	1.00373
Credit Deposit Ratio (%)	Pre-Merger	5	51.9860	6.70551	2.99879
	Post-Merger	6	72.9483	3.31435	1.35308
Investment ratio (%)	Pre-Merger	5	45.9680	3.83104	1.71329
	Post-Merger	6	33.5250	1.45352	.59340
Cash Deposit Ratio (%)	Pre-Merger	5	8.2780	1.14034	.50997
	Post-Merger	6	7.2150	1.12269	.45834
Divident Payout ratio	Pre-Merger	5	20.3400	2.33362	1.04363
	Post-Merger	6	24.4150	8.31206	3.39338
Return on Assets (%)	Pre-Merger	5	1.0680	.26771	.11972
	Post-Merger	6	.9317	.38881	.15873
Return on equity (%)	Pre-Merger	5	30.7080	3.84803	1.72089
	Post-Merger	6	19.8583	8.33152	3.40133

Conclusion:

A bank merger helps the institution to scale up quickly and gain a large number of new customers instantly. The markets seem to be in favor of bank consolidation. The Merger of BOB and IOB increased the number of branches as well as employee, assets and deposits.

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