Case Study

Mergers and Bank Performance in India: A Case on the State Bank of India

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Background of the Study

Prior to the initiation of financial reforms, Indian banks were operating in a highly regulated environment. In view of the social responsibility placed on the banking sector, profitability was not considered an important yardstick to judge their performance. From the time of nationalization of 14 major scheduled commercial banks in 1969 till the early 1990s, the main thrust of banking operation was on social banking. Accordingly, the emphasis was placed on enhancing branch network in rural and semi-urban areas. Moreover, banks had to undertake several other responsibilities which included the financing of fiscal deficit and facilitating the development of certain specific factors as reflected in high and increasing prescription of SLR and direct lending. With initiation of financial sector reforms, competition among the banks had increased. The competition is intense and irrespective of the challenge from the multinational players, domestic banks, both public and private, are also seen to be earnest in their pursuit of gaining competitive edge by opting for mergers and acquisitions. As a result, Mergers and Acquisitions (M&A) are the order of the day. As an aspect of strategic management, M&A can allow enterprises to grow, shrink, and change the nature of their business or competitive position. From a legal point of view, a merger is a legal consolidation of two entities into one entity, whereas an acquisition occurs when one entity takes ownership of another entity's stock, equity interests or assets. However, from a commercial and economic point of view, both types of transactions generally result in the consolidation of assets and liabilities under one entity, and the distinction between a "merger" and an "acquisition" is less clear.

Merger of SBI with its 5 associates namely State Bank of Bikaner and Jaipur (SBBJ), State Bank of Mysore (SBM), State Bank of Travancore (SBT), State Bank of Hyderabad (SBH), State Bank of Patiala (SBP) and Bharatiya Mahila Bank took place on 1 April, 2017. Shri Arun Jaitely is confident that the bank will become a global player due to this step of its merger with its five associate banks and Smt. Arundhati Bhattachary, Chairperson of SBI, expects that profits of the Bank shall increase by Rs. 3,000 crores in the coming 3 years. Therefore, the profitability performance of State Bank of India and its associates has become a fascinating topic for conversation, comment and debate. The approach of policy makers towards profitability has changed, with the result that low profits have become a fact of life. However, the economies of scale and scope have to be exploited for facing competition. Efficiency and profitability have, as a result, become critical objectives to be aimed at. Hence, in the present paper, an attempt has been made to analyze the profitability performance of SBI and its associates with the help of profitability ratios after completion of one year.

SBI at a Glance

State Bank of India (SBI) is an Indian multinational, public sector banking and financial services company. It is a government-owned corporation headquartered in Mumbai, Maharashtra. The company is ranked 217th on the Fortune Global 500 list of the world's biggest corporations as of 2017. It is the largest bank in India with a 23% market share in assets, besides a share of one-fourth of the total loan and deposits market. The Bank descends from the Bank of Calcutta, founded in 1806, via the Imperial Bank of India, making it the oldest commercial bank in the Indian subcontinent. The Bank of Madras merged into the other two "presidency banks" in British India, the Bank of Calcutta and the Bank of Bombay, to form the Imperial Bank of India, which in turn became the State Bank of India in 1955. The Government of India took control of the Imperial Bank of India in 1955, with Reserve Bank of India (India's central bank) taking a 60% stake, renaming it the State Bank of India. In 2008, the government took over the stake held by the Reserve Bank of India.

SBI and its Former Associate Banks

SBI acquired the control of seven banks in 1960. They were the seven regional banks of former Indian princely states. They were renamed, prefixing them with 'State Bank of. These seven banks were State Bank of Bikaner and Jaipur (SBBJ), State Bank of Hyderabad (SBH), State Bank of Indore (SBN), State Bank of Mysore (SBM), State Bank of Patiala (SBP), State Bank of Saurashtra (SBS) and State Bank of Travancore (SBT). All these banks were given the same logo as the parent bank SBI.

The plans for making SBI a single very large bank by merging the associate banks started in 2008, and in September the same year, SBS merged with SBI. The very next year, State Bank of Indore (SBN) also merged. In the same year, a subsidiary named Bharatiya Mahila Bank was formed. The negotiations for merging of the 6 associate banks (State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala, State Bank of Travancore and Bharatiya Mahila Bank) by acquiring their businesses including assets and liabilities with SBI started in 2016. The merger was approved by the Union Cabinet on 15 June 2016. The State Bank of India and all its associate banks used the same blue keyhole logo. The State Bank of India word mark usually had one standard typeface, but also utilized other typefaces.

On 15 February 2017, the Union Cabinet approved the merger of five associate banks with SBI. What was overlooked, however, were different pension liability provisions and accounting policies for bad loans, based on regional risks. The State Bank of Bikaner & Jaipur, State Bank of Hyderabad, State Bank of Mysore, State Bank of Patiala and State Bank of Travancore, and Bharatiya Mahila Bank were merged with State Bank of India with effect from 1 April 2017.

In the history of SBI it is not the first time when SBI has merged with other banks. Earlier in 2008, State Bank of Saurashtra was merged with SBI and in 2010 State Bank of Indore was merged with SBI.

Review of Literature and Identification of Research Gap

Beena P.L. (2000) attempted to analyze the significance of mergers and its characteristics. The paper suggested acceleration of the merger movement in the early 1990s is accompanied by the dominance of mergers between firms belonging to the same business group or houses with similar product lines.

Pramod Mantravadi & Vidyadhar Reddy (2007)'s study on the operating performance after mergers and acquisitions examined both pre-and post-merger financial ratios, with chosen sample firms, and all mergers involving public limited and traded companies of the nation between 1991 and 2003. The research suggested that there were minor variations in terms of impact on operating performance following mergers in different intervals of time in India. The study also indicated that for mergers between the same group of companies in India, there has been a deterioration in performance and return on investment, suggesting that such mergers were only motivated by potential for increasing the assets through consolidation of different businesses, rather than driving efficiency improvements.

A Kaleichelvan (2011) has looked at the M&A activity in the banking industry during the period 1993-94 to 2004-05. He found that the financial performance of both public and private sectors banks with respect to acquiring private limited banks does not result in any notable changes in its liquidity position as well as on its profitability levels. But the efficiency of the banks in generating income relating to their investment in fixed assets has declined in shorter time period. In addition, the net earnings in longer time period of five year tend to increase against taking over of private limited banks by public and private sector banks in India.

Subramanya Prasad has evaluated the post-merger efficiencies of Indian commercial banks (acquiring banks) which have undergone mergers during the post-reform period and analyzed the factors influencing the commercial bank efficiency in the Indian context and concluded with a positive note stating that the select bank's efficiency improved post merger

Anand Manoj & Singh Jagandeep (2008) studied the impact of merger on the shareholders of five banks: Times Bank with the HDFC Bank, the Bank of Madurai with the ICICI Bank, the ICICI Ltd with the ICICI Bank, the Global Trust Bank with the Oriental Bank of Commerce and the Bank of Punjab with the Centurion Bank. The study revealed that the announcement of merger of the banks had positive and significant impact on shareholders' wealth.

Sarangapani and Mamathaa (2008) examined some large Indian M&A deals were studied. The intent of the study was to understand the strategic intent behind M&A activity by analyzing the recent M&A in India. Intents of M&A using anecdotal evidence gathered from public statements of top management personnel in the media were analyzed. The data can be corroborated through collecting primary data from specific companies involved. This study can be furthered with a more detailed study of the M&A intents. Issues related to taxation and regulations are not within the scope of this work as data related to these were not available in the public domain. The propositions developed can be further tested over large sample sizes and temporally validated after three to five financial years. This can pave the way for a more detailed understanding of the corporate strategies of Indian firms, especially in times when more and more industries are maturing, leading to consolidation of players.

Kuriakose Sony & Gireesh Kumar G. S (2010) analyzed the strategic and financial similarities of merged banks, and relevant financial variables of respective banks and found that only private sector banks were in favour of voluntary mergers.

Azeem Ahmed Khan (2011) explored various motivations of Merger and Acquisitions in the Indian banking sector. The result of the study indicated that the banks have been positively affected by the event of merger and acquisitions. These results also suggested that merged banks could obtain efficiency and gains through Merger and Acquisitions and could pass the benefits to the equity shareholders' in the form of dividend.

Devarajappa S, (2012) explored various motives of merger in Indian banking industry. It also compared pre and post merger financial performance of merged banks with the help of financial parameters like, Gross Profit margin, Net Profit margin, Operating Profit margin, Return on Capital Employed, Return on Equity, and Debt Equity Ratio. Finally the study indicates that the banks have been positively affected by the event of merger.

The above review of literature points to the fact that studies have been made on mergers relating mainly to the performance of select banks; analysing the problems of mergers and benefits to the stakeholders; financial performance of the transferee bank after the merger. However, an analysis relating to Employee Productivity; Branch Productivity and the Profitability of the SBI before and after the merger till 31st March 2018 has not been done so far. Hence, the study is undertaken to fill the research gap.

Objectives of the Study

The objectives of the study are

- To study the reasons behind the merger of SBI with its five associated banks
- To analyse the employee productivity of SBI
- To analyse the branch productivity of SBI
- To analyse the post merger performance of SBI

Methodology

Sources of Data

The study is based on secondary sources which includes the Annual Reports of the SBI; RBI Database Profile of Banks –various issues; research publications, etc.

Period of Study

The period of the study is the post - liberalisation period, i.e. from 1st April 2014 to 31st March 2018.

Hypothesis

- H_o: There is no significant difference in the deposits per employee and per branch of SBI before and after merger.
- H_1: There is a significant difference in the deposits per employee and per branch of SBI before and after merger .
- H_o: There is no significant difference in advances per employee and per branch of SBI before and after merger.
- H_1: There is a significant difference in advances per employee and per branch of SBI before and after merger.
- H_o: There is no significant difference in the profits per employee and per branch of SBI before and after merger.
- H_1: There is a significant difference in the profits per employee and per branch of SBI before and after merger.

Tools for Analysis

The following tools are used for the analysis of the data apart from percentages and averages.

- *Employee & Branch Productivity ratios* for evaluating the employee efficiency and branch efficiency
- *CAGR*: to analyse the growth in deposits, advances and profits of the select banks
- *t test*: to test the Hypothesis as to whether there is any significant difference in the performance of the select banks before and after the merger.

Reasons of Merger

The reasons behind the merger of SBI with its associate banks and Bharatiya Mahila Bank are listed as follows:

- Government of India provides subsidy and contribution for bad debt recovery and share capital to SBI and its associate banks. It will become easy for government to provide aid to this single amalgamated bank instead of giving it separately to SBI and its associate banks.
- Profitability of SBI was going down for last few years and this merger will be able to show better position of profitability in the books of SBI. Net profit of the group fell from Rs. 12,225 crores in Financial Year 2016 to Rs. 241 crores in Financial Year 2017 and the losses were mainly due to associate banks.
- To recover loans which have turned bad and to reduce NPA of SBI and associate banks in future.
- For reconstruction of SBI and associate banks in the face of financial crises so that it can meet its liabilities
- With the merger, SBI has become bigger than before. Now it has a larger asset base and ranks 45th among top banks of the world.
- Management of the Bank will become easier as earlier all the branches were managed by separate managements though the holding was same and it used to make the whole process cumbersome.
- Cost of managing large number of branches will reduce which will increase profitability of the Bank.

Data Analysis

Pre & Post Merger Key Parameters of SBI

Table 1: Pre- and Post- Merger Key Parameters of State Bank of India

Year	Deposits	Advances	Net Profit	No of Employees	No of Branches
2014	1,394,408.51	1,209,828.72	10,891.17	222,033	16,059
2015	1,576,793.24	1,300,026.39	13,101.57	213,238	16,524
2016	1,730,722.44	1,463,700.42	9,950.65	207,739	16,784
2017	2,044,751.39	1,571,078.38	10,484.10	209,567	17,170
2018	2,706,343.29	1,934,880.19	-6,547.45	264,041	22,414
CAGR (%)	94.1	59.9	-160.1	18.9	39.6
Mean	1,890,603.77	1,495,902.82	7,576.01	223,323.60	17,790.20
Median	1,730,722.44	1,463,700.42	10,484.10	213,238	16,784
SD	514645.82	282663.87	7985.77	23416.96	2616.15
Skewness	1.19	1.00	-2.11	1.95	2.10
Kurtosis	1.16	0.88	4.58	3.86	4.54

Source: Compiled by the Author

Deposits advances; net profit, number of employees and branches of SBI four years before the merger and one year after the merger of State Bank of Saurashtra with itself in the year 2008-09 are presented in Table 1. The year of merger 2008-09 is taken as a base year for calculating CAGR. The deposits and advances of State Bank of Saurashtra at the time of the merger were Rs. 4,19,425 and Rs. 12,309.29 crores; net profit Rs. 35.45crores; employees was 7399 and the Bank had a network of 460 branches compared to that of SBI which had deposits of Rs. 7, 42,073 crores and advances of Rs. 5, 42,503 crores; 2, 05,896 crores of profits; had 12,022 employees and a branch network of 9,121. The deposits and advances of SBI, post merger grew by 11.92 % and 12.54% as against 13.22% and 18.97 % during the pre merger period. Profits have recorded a CAGR of 1.56 % as against pre merger CAGR of 21.30%. Number of Employees increased by 20% during the post merger period and its CAGR was in negative during the pre merger period and the number of branches increased by 4.04% as against 3.17 % during the pre merger period. It is evident from the above tables that there has been an increase in the two parameters of deposits and a advances all through; there is increase in the profits year after year excepting in the years 2013-14 and 2015-16; the number of branches increased during the overall study period excepting in the year 2002-03 during the pre merger period. With regard to the number of employees it is observed that from the year 1999-2000 there has been a consistent fall year after year in the number of employees during the pre and post merger periods with an exception in the years 2010-11 and 2012-13 and recorded a lowest growth rate of .20 % during the post merger period an against a negative growth rate of -3.00% during the pre merger period. The average increase during the pre and post merger period in deposits was Rs. 3,56,018.63 crores and Rs. 13,41,388.923 Crores. Advances were Rs. 2,18,545.86 crores and Rs. 11,05,807.851 crores. net profits were Rs. 3850.5 crores and Rs. 10,936.09 crores. The number of employees was 2,01,153.3 and 2,14,948.3. There was number of Branches 9420.75 and 15525.13. These figures only indicate the fact that, the Bank has been doing well, by generating increased amounts of deposits and disbursing increased amount of advances. T test is employed to see whether the difference in the key parameters before and after the merger is significant or not and the results are presented in table 4.

Table 2 t-Test Results of Key Parameters of State Bank of India

Year	Deposits	Advances	Net Profit	No of Employees	No of Branches
Pre-Merger Mean	1,686,668.90	1,386,158.48	11,106.87	213,144.25	16,634.25
Post-Merger Mean	2,706,343.29	1,934,880.19	-6,547.45	264,041.00	22,414.00
t Stat	-3.310783989	-3.02983	11.40568	-7.16713	-11.0845
t critical two tail	3.182446305	3.182446	3.182446	3.182446	3.182446
P two tail value	0.045365538	0.056319	0.001446	0.002798	0.001573
Source: Calculated on values in table1					

T test is employed to see whether the difference in the key Pparameters is significant or not for pre and post merger periods. The t stat values as per test at 5% significance level in case of all the parameters is less than the t critical two tail value; p value less than .05, indicating that there is a significant difference in their performance, rejecting the null hypothesis. As seen in the above table over a period of sixteen years, eight years before the merger and eight years after the merger, changes were witnessed in the parameters and the t test results indicated that the change is significant.

Conclusion

Merger is considered as a strategic tool for its participants for realising growth through synergy. Since liberalisation in 1991, twenty - three bank mergers have already taken place in the Indian context. The objective of this study was to analyse the performance of State Bank of India in pre and post merger period through certain selected key parameters like deposits, advances, net profit, number of employees and number of bank branches. Descriptive analysis of the data corresponding to these selected key parameters revealed an increasing trend in deposits, advances, number of employees and number of bank branches except net profit. The deposits and advances of SBI post merger grew by 11.92 % and 12.54% as against 13.22% and 18.97 % during the pre merger period; profits have recorded a CAGR of 1.56 % as against pre merger CAGR of 21.30%; the number of employees increased by .20% during the post merger period and its CAGR was in negative during the pre merger period; and the number of branches increased by 4.04% as against 3.17 % during the pre merger period. Furthermore, the results of t-test revealed a significant difference in performance during pre merger and post merger periods for State Bank of India.

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