

Merger and Acquisition Effect on Financial Performance of SBI

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ABSTRACT

The banking system is the lifeblood of any country's financial system. Without an efficient banking system, a country will not be able to face the complex environment of the outside world. This study compares the pre-post financial performance of SBI and its Associates (SBI Consolidated) using 'ROE,' 'Debt-Equity ratio,' 'Return on long term funds,' 'Interest Income to Total Income' and 'Total Advances to Total Assets.' The study covers four years, -2yrs merger and +2yrs merger. The findings revealed that all the ratios under study observed insignificant t-value; thus, there are no significant changes in the period after the merger compared to the pre-merger period. However, these conclusions are merely based on observations that could not accurately present the impact of the merger on the State Bank of India.

Keywords: Mergers and Acquisitions; Financial performance

1. INTRODUCTION

Banks have become a crucial piece of our lives, from setting aside cash to reserve tickets and advancing cash-related activities. Banks have become the extension that interfaces us with cash. Banks are located physically, with customers using banking services like ATMs and safety deposit boxes. However, many banks started to operate online this time, and all the transactions with a commercial bank were done electronically.

1.1. Concept of Mergers and Acquisitions

Merger and acquisition is an umbrella phrase for integrating enterprises or resources using various monetary considerations, including combinations, amalgamations and takeovers. The terms “mergers” and “acquisitions” are frequently used interchangeably, though they are both separate terms with different meanings. With the goal of abundance augmentation, organizations continue to assess various freedoms through M & A (Nelson, 2018).

1.1.1. Acquisitions

Whenever one business takes control of the other and acquires its ownership, this purchasing behavior is called acquisition. From the legal point of view, the target organization's identity no longer exists, the acquirer takes over the enterprise, and the bidder firm's securities continue to be traded in the market. In contrast, the acquired organization's stocks are no longer traded in the market.

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1.1.2. Mergers

In contrast to the acquisition, a merger occurs when two roughly comparable-sized enterprises join forces to move forward as a single new entity rather than remaining separate entities. It is known as an "amalgamation of companies." The securities of both the companies are surrendered, and the new entity's securities are issued instead of old firms. For example, X Ltd and Y Ltd. ceased when the two companies were combined. A new entity, XY Ltd, is formed. The agreement of combining two firms is also called a merger.

2. Types of Mergers and Acquisitions

2.1. Horizontal Mergers

Horizontal mergers happen when one company merges or gets possession of another company that provides the same or comparable product offerings and administrations to the last purchasers, implying that they are in the same industry and at the same stage of development. Companies are often immediate contenders in this case. For example, if a company that makes PDAs merges with another company that makes mobile phones, this is a horizontal merger. The benefit of this type of consolidation is that it eliminates competition, which pushes the organization to grow its share of the total industry, earnings, and profits (Hanson, 2016).

2.2. Vertical Mergers

A vertical merger is performed to connect two organizations with comparable worth and provide comparable services, with the sole difference being the stage of production at which they are functioning. For example, if a clothing store acquires a material manufacturing factory, this is a vertical merger because the business is similar. However, the creation phase is distinct: one entity works in the tertiary region while another operates in the optional region. These mergers are commonly used to ensure the supply of essential products and avoid interruptions in

supply. E.g., the clothing store can be confident that apparel will be delivered by the material manufacturing plant (Hanson, 2016).

2.3. Concentric Mergers

Concentric mergers happen when two companies serve closely related clients in the same industry but do not offer the same products and services. Their products may complement one another but are not identical. These are typically used to entice buyers because it is easier to sell them together. Trying to sell one of the products will also facilitate the sale, resulting in increased revenue for the establishment. These mergers allow companies to venture into new business areas, reducing uncertainty and accessing previously inaccessible resources and markets (Hanson, 2016).

2.4. Conglomerate Mergers

When two companies work in a completely distinctive industry, a merger is known as a conglomerate merger regardless of the development stage. For instance, a watchmaker getting a concrete producer, a steelmaker procuring a product organization, and so on, the fundamental target of a combination merger is to accomplish a significant size. This is typically done to enhance different businesses, decreasing risk (Hanson, 2016).

2.5. Reverse Mergers

A reverse merger is an appealing vital choice for privately-owned supervisors to acquire public organization status. It is a less tedious and less exorbitant option than the usual initial public offerings (IPOs). The public organization appreciates more prominent adaptability regarding financing choices, and the organization's financial backers appreciate more significant liquidity. Public organizations face extra consistency loads and guarantee that adequate time and energy remain committed to running and becoming the business. A fruitful reverse merger can expand the estimation of an

organization's stock and liquidity (Sjostrom, 2007).

2.6. Hostile Takeover

A forced or hostile takeover is an acquisition of a company called the target company by the other company known as the acquirer. The later company forcibly gains access to the organization's resources and replaces the top management body of the company. A hostile takeover can be prevented or avoided by making a delicate offer or implementing counter-strategies. Sometimes a company's management will use dubious practices, such as the 'poison pill,' 'the crown-jewel safeguard,' a 'hangout,' or 'the Pac-Man defense,' to protect against unwanted hostile takeovers (Ganti, 2021).

3. Review of Literature

Ishwarya (2019), in her research "*Study on Mergers and Bank Acquisition: A Case Study on SBI and its Associates,*" examined the banks' before and after merger financial performance utilizing specific financial parameters. The study also observed the trends in mergers and acquisitions in the Indian banking sector. The analysis revealed no significant alterations in the profitability of the post-merger period. Research findings indicated that the merger between a strong bank and a distressed bank did not prove beneficial to a substantial bank as it was to a sick bank.

Rehan et al. (2018), in their research "*Effects of Merger and Acquisition on the Profitability of Banks,*" used a collection of nine pre & post-merger and acquisition Pakistan's bank data from 1996 to 2016. For research purposes, pre-post mergers and acquisition status were compared using metrics such as "Gross Profit Margin," "Net Profit Margin," "Return on Capital Employed," and "Debt-Equity Ratio." The paired sample t-test was employed to evaluate the effect before and after the merger and acquisition. It was recommended by the study

that all the banks should minimize their gross profit margin for the improvement of financial performance and efficiency and also suggested to pay attention to increasing capital efficiency and should rely more on equity financing than debt.

Kumar and Murty (2017), in their research "*Financial Performance of selected Public and Private Sector Banks based on CAMEL model concerning Indian Banking Sector,*" examined the financial soundness of banks (public and private) using the CAMEL model from 2012 to 2016. For the analysis, two public sector banks were used as samples, i.e., SBI and Bank of Baroda and two private sector banks, viz. 'ICICI Bank' and 'AXIS Bank.' The selected banks were analyzed based on CAMEL parameters and ranked for each parameter. The results have shown that ICICI should strengthen its role in terms of Asset quality and capital adequacy. SBI must strengthen its liquidity while the Bank of Baroda should strengthen its earnings quality. The study also found that, while the ratios differed for various banks in the selected private and public sectors, there was no statistical difference in the CAMEL ratios.

Shrestha et al. (2017) conducted an "*A comparative study of merger effect on the financial performance of banking and financial institutions in Nepal.*" Six financial institutions and banks were chosen to be sampled for the analysis, alongside 120 respondents were interviewed for the data. The analysis used eight financial ratios to evaluate the bank's pre-and post-merger financial results. A paired sample t-test was employed to observe the changes due to mergers in the financial performance of commercial banks. The study shows that the merger is optimistic when the bidder banking and financial institutions are commercial banks of a relatively large scale. The efficiency of the loan decreased substantially after the merger, and the profitability calculated in terms of ROA and ROE was

negatively affected in some instances just after the merger. The study also points out that mergers and acquisitions can be achieved by recognizing the need rather than pushing it.

Satyanarayana et al. (2017), in their study on “A case study on mega-merger of SBI with its five Subsidiaries,” explored the factors that triggered the merger of SBI with its five Associate banks and also attempted to evaluate the challenges and opportunities of Mega-merger. It is suggested that there are several economic and strategic advantages to the merged entity. However, the new entity is not free from challenges. It must gear up to face new challenges to come in the future.

Njogo (2016), in the study “*The Impact of Mergers and Acquisitions on the Performance of Deposit Money Banks in Nigeria*,” assessed the financial performance of ten banks over the period ranging from 2001 to 2010 using nine variables. The research examined the bank's pre and posted mergers and acquisitions, employing a paired sample t-test sample. The findings revealed a considerable difference in the performance of deposit money banks on Return on Assets, Return on Equity and leverage ratios in the pre and post-merger periods, but that there was not much impact on the position of deposit money banks on other variables.

Tanwar (2016) examined Indian banks' performance in the period of M&As. The paper examined the “*Financial and Operating Performance of merged banks from 2006-2010*”. The CAMEL method was employed to assess the financial performance of acquiring banks before and after the merger. Statistics like mean, standard deviation, and coefficient of variance were analyzed to examine the variation in the bank's performance from a pre-merger situation. The findings revealed a considerable difference in the merged institutions' overall performance during the merger period.

Singh and Gupta (2015), in a paper titled “*An impact of mergers and acquisitions on productivity and profitability of consolidation banking sector in India*,” examined the effects of M&A's on profitability as well as a productivity based on fourteen ratios, which compared the before and after merger status of identified banks (public and private) from 2004-05 to 2014-15. The study covers a public sector bank merger between SBI and State Bank of Saurashtra, held in 2008 and a private sector bank merger between ICICI Bank and Bank of Rajasthan, held in 2010. A t-test, mean, standard deviation, and p-value were employed to compare selected bank mergers' financial performance. The study revealed a rise in the post-merger financial performance of banks being studied.

Gupta (2015), in the research “Mergers and Acquisitions in the Indian Banking Sector: A Study of Selected Banks,” assessed the impact of mergers and acquisitions upon the financial performance of certain banks. Two bank mergers were taken as a sample, viz. ‘ICICI Bank-The Bank of Rajasthan’ and ‘HDFC bank-Centurion Bank of Punjab.’ The research compared the before and after financial merger results based on different ratios and parameters. The study tried to find the discrepancy in the financial results, pre and post the merger, using t-Test. The research results showed that the financial performance of selected banks improved compared to the pre-merger period.

Duggal (2015), in her paper “*Mergers and Acquisitions in India: A Case Study on Indian Banking Sector*,” focused on understanding the effects of mergers on the bank's financial performance. The research considered only eight public sector banks' mergers announced from January 2001 to December 2006. The result showed that analyzing different financial ratios for a three-year pre-period and five years post- period using t-test with a 0.05 level of confidence. A significant effect was noticed in return to asset ratio, as most banks

reported significant results. At the same time, ROE and EPS turn out to be the least performing ratios. ROCE and Net Profit Margin showed a significant improvement.

Singh (2015) undertook a study, “*An analysis of the profitability position of a private bank in India*,” focused on the profitability ratio including "Interest Spread," "Net Profit Margin," "Return on long-term funds," "Return on Net Worth," "Return on assets," and "Adjusted Cash Margin." The researcher has used statistics like mean, standard deviation, coefficient variance and ANOVA as statistical analysis tools. According to the study, there was no significant relationship between the identified Indian private sector banks regarding the above ratios.

Masud (2015) emphasized the “*impact of merger and acquisition on the financial performance of banks*.” To examine this effect, three banks were selected that merged during 2005-2011, but data was gathered from 2000-2012. Financial performance is measured based on ROA & ROE, and paired t-test was used to examine the bank's performance. The study showed a decline in financial performance in the first year of the merger, but after that, it increased slightly and continued to rise.

4. Mergers & Acquisitions Of Various Public Sector Banks In The Period 2008-2020

- On 13th August 2008, ‘State Bank of Saurashtra’ was merged into SBI. At that time, the State Bank of Saurashtra had 423 branches stretched in more than 15 states. State Bank of Indore was authoritatively converged into SBI on 26th August 2010 and had more than 470 branches over 300 urban areas and towns at the hour of consolidation. SBI was converged with the remaining five Associate banks in April 2017 alongside Bhartiya Mahila Bank.

- On 1st April 2019, ‘Dena Bank’ and ‘Vijaya Bank’ were merged into ‘Bank of Baroda.’ This merger was beneficial for the banks' shareholders as they were provided 110 and 402 equity shares, respectively, of Rs 2 for every 1000 shares they had of Bank of Baroda.
- ‘Oriental Bank of Commerce’ and ‘United Bank of India’, on April 1, 2020, merged with Punjab National Bank. Shareholders in both banks received 1150 shares of PNB and 121 shares of PNB for every 1000 shares they held. As a result of this merger, PNB became the country’s second-largest public sector bank.
- Canara bank is expected to power over Syndicate Bank on first April 2020. Partner Bank investors got 158 value shares for every 1000 offers held in Canara Bank.
- In April 2020, ‘Andhra Bank’ and ‘Corporation Bank’ was merged into ‘Union Bank of India.’ After consolidation, ‘Union Bank of India’ has become the fifth most prominent public sector bank with resources of Rs. 14.59 lakh crore and 9609 branches in various sections of India.
- On first April 2020, Allahabad Bank was merged into Indian Bank. The consolidation has made the country's seventh biggest public sector bank with resources worth Rs. 8.08 lakh crore.

5. Research Methodology

The current study attempts to measure, assess, and compare SBI and its associate banks' financial performance using ‘Return on Equity,’ ‘Debt-Equity Ratio,’ and ‘Return on Long Term Assets,’ ‘Interest to Total Assets,’ and ‘Total Advances to Total Assets.’ Because India's largest bank merger of public and

private sector banks opens up many research opportunities.

5.1. Objectives of the Study

The present study has two primary objectives, mentioned as follows:

1. To examine the before and after merger financial performance of SBI and its Associate (SBI consolidated)
2. To identify the reasons and effects of the merger of SBI and its Associate (SBI consolidated)

5.2. Collection of Data

Secondary data is used for the study. Secondary data corresponds to data obtained by someone other than the primary/current researcher/user (Schutt, 2006). The data is gathered from Annual reports of SBI and its Associate Banks, RBI website, moneycontrol.com and various statements and reports, and books and journals.

6. Data Analysis

6.1. Reasons for Merger of SBI with its Associate Banks

Regardless of whether it is an assembling organization or administration association, the fundamental reason for any association is to develop year on year as far as benefits and client base. The associations should be proficient at dealing with their activities and fulfilling their clients to build benefit. Associations, including banks, are falling back on mergers and acquisitions to address expanding rivalry, diminish the general expense of activities, increment productivity, and increase benefit. The fundamental reason for mergers and obtaining action is to bring collective energy between two elements. Following are the purposes behind the mergers.

- The government of India gives appropriation and commitment to imperfect obligation recuperation and offers cash flow to SBI and its partner banks. It then will turn out to be simple for the government to help this single amalgamated bank instead of giving it independently to SBI and its partner banks.
- SBI's profitability has been declining for several years, and the combining of will want to represent a better situation of profits in SBI's books. The group's net profit fell from Rs. Twelve thousand two hundred twenty-five crores in the Fiscal Year 2016 to Rs. Two hundred forty-one crores in the Fiscal Year 2017, owing primarily to partner banks.
- The merger of SBI with its associate banks was critical to recovering bad loans and reducing the NPA of SBI and its associate banks in the future.
- SBI and its partner banks will meet their obligations in a monetary emergency.
- SBI has developed more than before as a result of the mergers. It now has a large capital base and ranks among the top 50 banks globally.
- Managing the bank will become relatively simple, as previously, all branches were supervised by autonomous administration, but the owner was the same, making the entire cycle cumbersome.
- The cost of supervising an extensive network of branches will significantly reduce, increasing bank efficiency.

6.2. Results

The following results were obtained with the available data analysis.

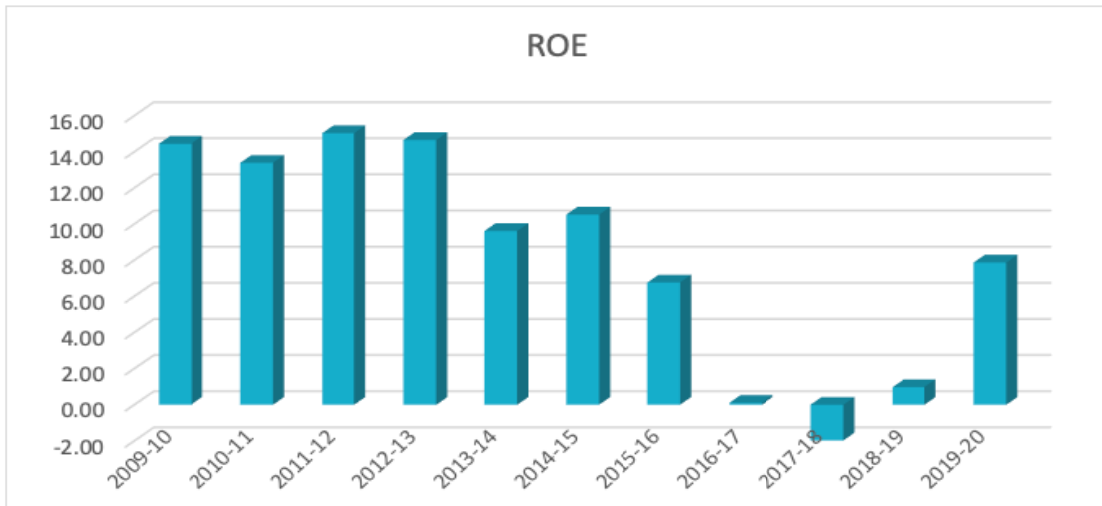


Figure 1: Return On Equity (Source: Annual Reports of State Bank of India Group)

Table 1: Mean Comparison on the Return on Equity

Returnon Equity	Mean	SD	t-values (4)	Sig
Pre-Merger	-20.20	25.72	.411	Insights
Post-Merger	-342.87	1360.55		

The above table gives the mean Comparison of return on equity; in the pre-merger situation, return on equity is (M = -20.20, SD=25.72) while for post-merger, the same is (M=-342.87, SD=1360.55), which shows a significant difference in mean on the other hand if one looks at the t-value as it stands to be insignificant (t(4)=.411, p=.702) which shows no significant difference amongst pre and post-merger conditions.

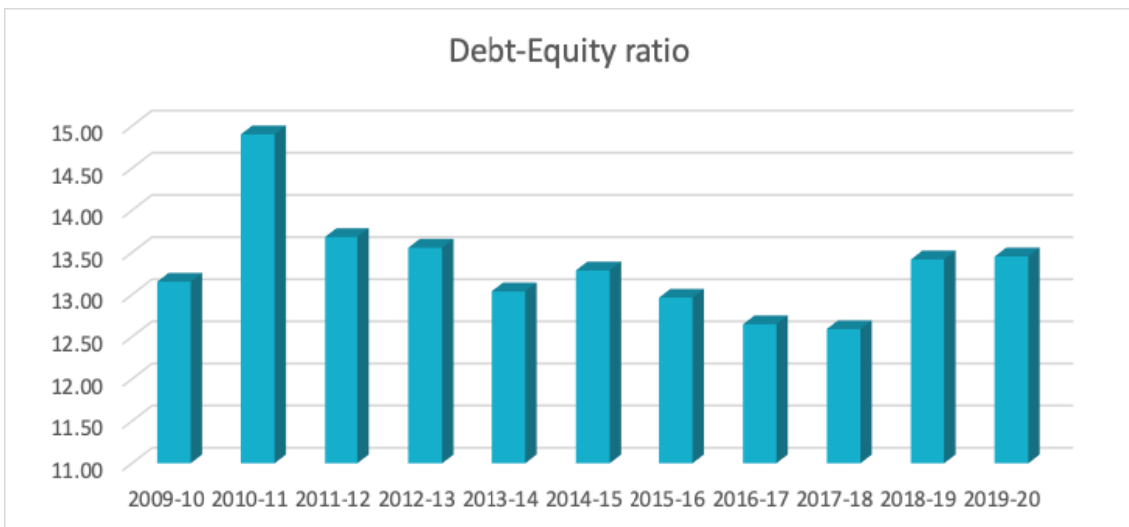


Figure 2: Debt Equity Ratio (Source: Annual Reports of State Bank of India Group)

Table 2: Mean Comparison On Debt-Equity Ratio

Debt Equity Ratio	Mean	SD	t-values (4)	Sig
Pre-Merger	-1.44	2.98	-1.26	insight
Post-Merger	2.12	3.85		

The above table gives the mean Comparison of the debt-equity ratio; the pre-merger period debt-equity ratio is (M=-1.44, SD=2.98) while for post-merger, the same is (M=2.12, SD=3.85), which shows a significant difference in mean on the other hand. Further, the t value stands to be insignificant (t(4)=-1.26, p=.274), which shows no significant difference between pre and post-merger conditions.

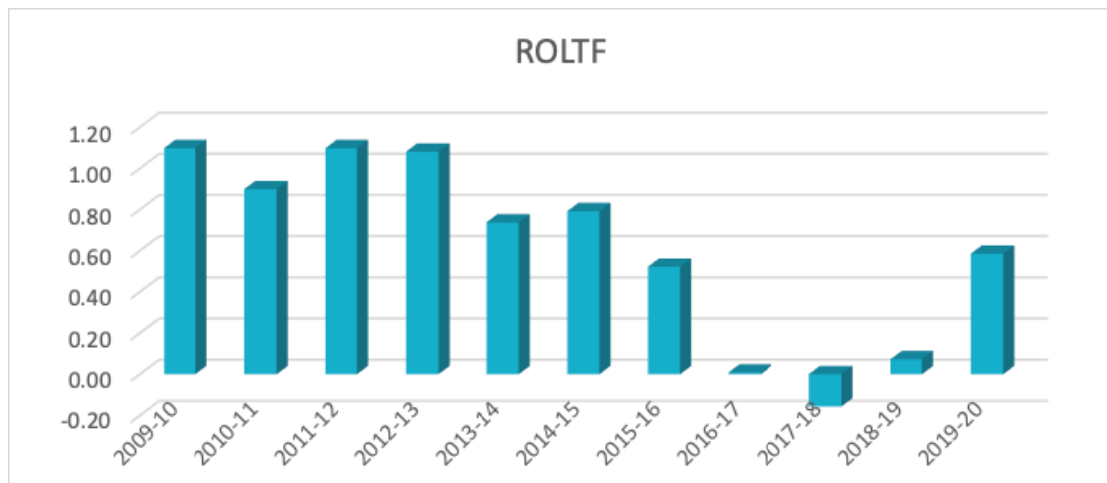


Figure 3: Return on Long Term Fund (Source: Annual Reports of State Bank of India Group)

Table 3: Mean Comparison on Return on Long Term Funds

Return on Long Term Funds	Mean	SD	t-values (4)	Sig
Pre-Merger	-19.47	23.34	.416	Insights
Post-Merger	-347.28	1363.75		

The above table gives the mean Comparison of return on long-term funds; in pre-merger situations, return on long-term funds is (M=-19.47, SD=23.34) while for post-merger, the same is (M=-347.28, SD=1363.75), which shows a significant difference in mean on the other hand. Further, the t value stands to be insignificant (t(4)=.416, p=.699), which shows no significant difference between pre and post-merger conditions.

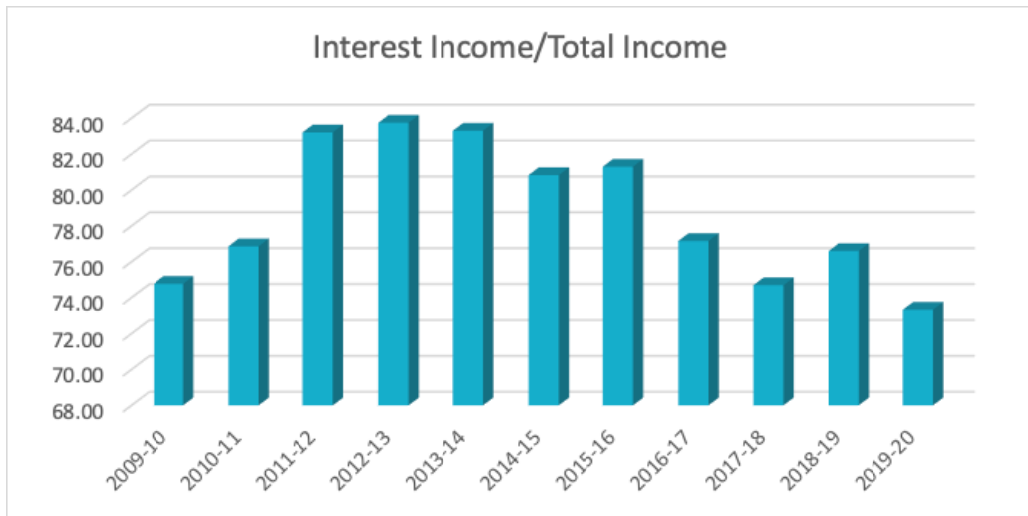


Figure 4: Interest Income/Total Income (Source: Annual Reports of State Bank of India Group)

Table 4 : Mean Comparison on Interest Income to Total Income

Interest Income to Total Income	Mean	SD	t-values (4)	Sig
Pre-Merger	-.973	1.81	.283	Insights
Post-Merger	-1.64	3.67		

The above table gives the mean Comparison of interest income to total income; if we see the above table, we will find that interest income to total income is (M=-.973, SD=1.81) in the pre-merger situation while for post-merger same is (M=-1.64, SD=3.67) which shows mean difference. However, it is not significant, which is also shown by (t(4)=.283, p=.791), indicating no significant difference between pre and post-merger conditions of the ratio.

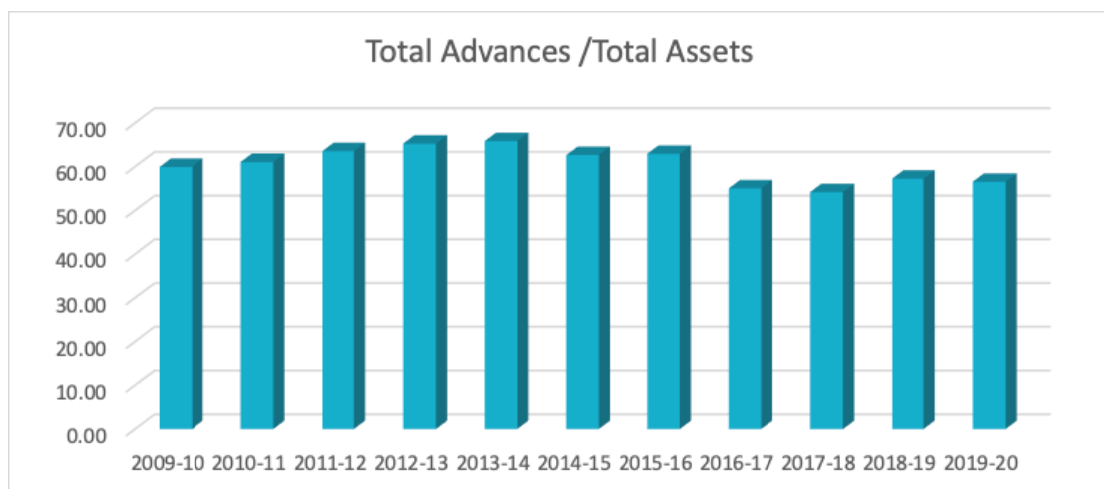


Figure 5: Total Advances/Total Assets (Source: Annual Reports of State Bank of India Group)

Table 5: Mean Comparison on Total Advances to Total Assets

Total Advances to Total Assets	Mean	SD	t-values (4)	Sig
Pre-Merger	-1.17	3.20	-.710	Insights
Post-Merger	.95	4.07		

The above table gives the mean Comparison of total advances to total assets; in the pre-merger situation, total advances to total assets is (M=-1.17, SD=3.20), while for post-merger same is (M=.95, SD=4.07), which shows a significant difference in mean. Further, the t value stands to be insignificant (t(4)=-.710, p=.517), which shows there is not much difference in both the conditions.

Conclusions

The study shows that the financial performance of the State Bank of India has not shown much significant difference post-merger period. All the ratios understudy, 'Return on Equity,' 'Interest Income to Total Income,' 'Debt-Equity ratio,' 'Return on Long term funds,' and 'Total Advances to Total Assets ratio' seems to be experienced no change from the pre-merger period. However, these conclusions are merely based on observations that could not accurately present the impact of the merger on the State Bank of India.

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