MERGERS AND ACQUISITION IN BANKING SECTOR:

A Research Paper submitted in partial fulfilment for the requirement of the Internship, June 2013

SUBMITTED TO:

Mr Rajinder kumar
Deputy Director (Economics)
Competition Commission of India

SUBMITTED BY:

Jagriti kumari
M.Sc. Environment Economics (1st year)
Madras School of Economics
ACKNOWLEDGEMENT

I take this opportunity to express my gratitude towards my Guide, Shri Rajinder Kumar for extending to me all possible help during my internship at the Commission. This project would not have been possible without his help and guidance. Apart from guiding me throughout, he gave me utmost freedom and liberty in carrying out my research. I would like to thank the Librarian and all other staffs for providing access to all the relevant books from the library. I thank other officials and office staffs, who have also extended their help whenever needed. I thank my co-interns at Competition Commission of India for helping me, whenever I needed help. I would also like to thank the Competition Commission of India for providing me with this opportunity.
## CONTENTS

<table>
<thead>
<tr>
<th>CHAPTER</th>
<th>PAGE NUMBER</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CHAPTER-1</strong></td>
<td></td>
</tr>
<tr>
<td>- INTRODUCTION TO INDIAN BANKING SYSTEM</td>
<td>4</td>
</tr>
<tr>
<td>- INTRODUCTION OF CCI</td>
<td>6</td>
</tr>
<tr>
<td><strong>CHAPTER-2</strong></td>
<td></td>
</tr>
<tr>
<td>BANKING REFORMS IN INDIA</td>
<td></td>
</tr>
<tr>
<td>- NARSIMHAN COMMITTEE REPORT-2</td>
<td>7</td>
</tr>
<tr>
<td>- RAGHURAM RAJAN COMMITTEE</td>
<td>9</td>
</tr>
<tr>
<td><strong>CHAPTER-3</strong></td>
<td></td>
</tr>
<tr>
<td>NETWORK ECONOMICS IN BANKING SECTOR</td>
<td>10</td>
</tr>
<tr>
<td>MARKET STRUCTURE AND HHI</td>
<td>12</td>
</tr>
<tr>
<td><strong>CHAPTER-4</strong></td>
<td></td>
</tr>
<tr>
<td>- CLASSIFYING MERGER</td>
<td>13</td>
</tr>
<tr>
<td>- REASONS FOR MERGER</td>
<td>14</td>
</tr>
<tr>
<td>- IMPACT OF MERGER</td>
<td>15</td>
</tr>
<tr>
<td><strong>CHAPTER-5</strong></td>
<td></td>
</tr>
<tr>
<td>- HISTORY OF BANKING Mergers IN US AND EU</td>
<td>16</td>
</tr>
<tr>
<td>- MAJOR CASES WHICH RAISED COMPETITION ISSUES IN US &amp; EU</td>
<td>18</td>
</tr>
<tr>
<td>- MAJOR FINDINGS</td>
<td>22</td>
</tr>
<tr>
<td><strong>CHAPTER-6</strong></td>
<td></td>
</tr>
<tr>
<td>- MERGER AND ACQUISITON EXPERIENCE OF INDIA</td>
<td>22</td>
</tr>
<tr>
<td>- WHY THERE IS A NEED OF CONSOLIDATING MARKET</td>
<td>25</td>
</tr>
<tr>
<td><strong>CHAPTER-7</strong></td>
<td></td>
</tr>
<tr>
<td>CREATING A HYPOTHETICAL SCENARIO</td>
<td>26</td>
</tr>
<tr>
<td>- ANALYSIS OF MARKET SHARE AND COMPETITION ISSUES IF FIVE BIG PUBLIC SECTOR BANKS MERGE</td>
<td></td>
</tr>
<tr>
<td><strong>CONCLUSION</strong></td>
<td>31</td>
</tr>
<tr>
<td><strong>RECOMMENDATION</strong></td>
<td>32</td>
</tr>
<tr>
<td><strong>REFERENCES</strong></td>
<td>33</td>
</tr>
</tbody>
</table>
CHAPTER-1

INTRODUCTION TO INDIAN BANKING SYSTEM:

OBJECTIVE- Here our main objective is to analyse the impact of mergers and acquisition in banking sector in India. We will try to find out from the experience of US and EU how Indian banking sector will respond if some major players merge together. In this report we will create a situation in which five big players in banking sector merge together and we will analyse the effect of merger on Indian Banking sector.

In the past three decades, India's banking system has earned several outstanding achievements to its credit. The most striking is its extensive reach. It is no longer confined to metropolises or cities in India. In fact, Indian banking system has reached even to the remote corners of the country. This is one of the main aspects of India's banking growth story. The first banks were Bank of Hindustan (1770-1829) and The General Bank of India, established 1786 and since defunct.

The largest bank, and the oldest still in existence, is the State Bank of India, which originated in the Bank of Calcutta in June 1806, which almost immediately became the Bank of Bengal. This was one of the three presidency banks, the other two being the Bank of Bombay and the Bank of Madras, all three of which were established under charters from the British East India Company. The three banks merged in 1921 to form the Imperial Bank of India, which, upon India’s independence, became the State Bank of India in 1955.

The Government of India issued an ordinance and nationalised the 14 largest commercial banks in 1969. These banks have 85 per cent of bank deposits in the country. A second round of nationalisation of 6 more commercial banks took place in 1980. Nationalisation took place so that government get more control of credit delivery. With the second round of nationalisation, 91% of banking business was held by the Government of India. Later on, in the year 1993, the government merged New Bank of India with Punjab National Bank. It was the only merger between nationalised banks and resulted in the reduction of the number of nationalised banks from 20 to 19.

ERA OF REVOLUTION IN BANKING:

IT IN BANKING- Information and communication technology has brought a transformational change in banking operations and payment systems in banks.

Core Banking Solution (CBS) - With Core Banking Solution, banks can effectively meet challenges of reducing operational cost and establishing customer intimacy.

Automated teller Machines - Now with the huge network of ATMs there is no need for the customers to visit the bank branches and stand in long queues to withdraw or deposit money.

Smart Cards- It is popularly known as plastic money. These pocket sized integrated circuit embedded cards have eliminated the need for paper money.
Internet Banking - It has eliminated the need to visit bank branch to a great extent. Just sit in the comfort of your house and customers can perform any banking transaction.

MICR and automated cheque clearing - Magnetic ink character recognition (MICR) allows computers to read the number printed on the cheque. Eliminated human errors. This saved

1 The time required to transfer cheques from one city to other and reduced the cheque clearing time from 3 days to 1 day.

Mobile banking - his has further increased the ease for a bank’s customer. Now the customer does not require a pc or laptop to get in connection with his bank.

RFID in Banks – usage of RFID technology for the better customer relationship management. New tech savvy banks like YES bank use this technology for its customers so that it can give a personal touch to its customers when they enter its premises.

Bank2.0 - Bank2.0 seems to be the future of banking. Banks can start maintaining their own blogs, create financial forums, provide video tutorial and video calling and engage in community banking.

Banks actually need to provide a platform for interaction among its customers.

COMPETITION COMMISSION OF INDIA

Competition is a basic mechanism of the market economy and it encourages companies to provide consumer products according to their preferences. The explanation for competition law or policy is ultimately and essentially to improve consumer welfare. Main objective is to improve production.

Competition Commission of India is a body of the Government of India responsible for enforcing The Competition Act, 2002 throughout India and to prevent activities that have an adverse effect on competition in India. The Competition Act, 2002 has been enacted with the purpose of providing a competition law regime that meets and suits the demands of the changed economic scenario in India. The Competition Commission of India (CCI) has drawn the Reserve Bank of India’s

1 http://en.wikipedia.org/wiki/Banking_in_India
(RBI's) attention to distortions in banking due to a limited presence of the private sector, high entry barriers for foreign banks and cartelisation of sorts among banks in setting interest rates.

The commission does not have statutory backing but the issues raised by it are likely to create some trouble. Mergers are those forms of business transactions where there is a combination of two or more corporate entities, and in the process of combining of two entities one or more such corporate entities lose their corporate existence because they merge with the surviving entity. Acquisitions are those forms of business transactions where the shares or control of a company is taken over by persons who, prior to the change in the shareholding or control, did not possess such shareholding or control. The Competition Commission of India (CCI) has drawn the Reserve Bank of India's (RBI's) attention to distortions in banking due to a limited presence of the private sector, high entry barriers for foreign banks and cartelisation of sorts among banks in setting interest rates.
CHAPTER-2

BANKING REFORMS IN INDIA:

NAR SIMHAN COMMITTEE REPORT²

The Narsimhan Committee on Banking Sector Reform was set up in December, 1997. This Committee’s terms of reference include; review of progress in reforms in the banking sector, to make banking system robust and internationally competitive reforms should be modified according to situations, framing detailed recommendation regarding banking policy for each dimension like institution, technology and legislative. The Committee submitted its report on 23 April, 1998 with the following suggestions:

1) Use of mergers to build the size and strength of operations for each bank.

2) Recommended merger of larger Indian banks to make them strong enough to stand in international trade.

3) Speed up computerization in PSB.

4) Strengthen legal framework for credit recovery.

5) There should be two to three banks with international orientation, eight to ten national banks and a large pool of local banks so that system can cover remote areas too.

6) Narrow banking will help weak banks to recover large banks should merge only with banks of equivalent size and not with weaker banks.

7) Confine small, local banks to States or a cluster of Districts.

8) Review the recruitment procedures, and the training and remuneration policies of PSU bank.

9) Enhanced banking risk can be matched with increased capital adequacy.

10) Budgetary support non-viable for recapitalization.
11) No alternative to the asset reconstruction fund.2

12) Review the RBI Act, the Banking Regulation Act, the Nationalization Act and the State Bank of India Act.

13) Professionalization of the bank Boards.

**RAGHURAM RAJAN COMMITTEE: A HUNDRED SMALL STEPS**

In April 2009, Raghuram Rajan penned a guest column for *The Economist*, in which he proposed a regulatory system that might minimize boom–bust financial cycles.

The Terms of Reference of the Committee will be as follows:

(i) We need to identify the changes required in our supervisory infrastructure and regulatory infrastructure that will allow financial sector to play a better role by keeping the risk factor intact.

(ii) To analyse the financial sector and its various segments and analyse the changes to meet the requirements of real sector.

(iii) To analyse changes in other segments of the economy and it includes the conduct of Monetary and Fiscal policy and operation of legal and educational framework that will help financial sector to work effectively and efficiently.

(iv) To analyse the challenges in financial needs that will crop up in coming years and to meet those challenges effectively we need real sector reforms.

**SUGGESTIONS BY RAGHURAM RAJAN COMMITTEE:**

- Deregulation is required in certain areas.

- Given how open India is, it is impossible to control capital flows and it will create uncertainty and volatility in economy.

- To grow into large banks there is a need to offer an entry point in banking systems which entities can use.

- Priority sector lending services certificates

---


3 [http://planningcommission.nic.in/reports/genrep/report_fr.htm](http://planningcommission.nic.in/reports/genrep/report_fr.htm)
-> Advancement in technology can help some small banks to evolve and reduce its operational cost.

-> Greater participation of foreign players in domestic markets.

-> Give proper incentive and encouragement to professional markets.

-> Reduced government ownership below 50% still maintaining its control

-> Selling of small underperforming PSUs.

-> Stop or reduce creating uncertainty for investors by banning markets.

-> Bringing trade regulations under SEBI.

-> Creating an innovation friendly environment for investors.

-> More liberal perspective in mergers and takeovers.
CHAPTER-3

NETWORK ECONOMICS IN BANKING SECTOR:

Banking systems are consolidating many markets and banks and also extending their presence across borders. Financial conglomerates are gaining importance. New financial services providers are emerging, including online-only banks and brokerages, and companies that allow consumers to compare financial services more easily as to price and quality (eBay, ivillage)\(^4\)

Financial services are also dependent on networks for their production and distribution which makes competition policy necessary. Banking systems are consolidating in many markets and banks are extending their presence across borders. Financial conglomerates are increasing in importance. New financial services providers are emerging, including online-only banks and brokerages, and companies that allow consumers to compare financial services more easily as to price and quality.

Main characteristics of networks and related public policy issues\(^3a4\)

- **Economies of scale on supply side**- Network property states that physical network infrastructure is developed by one entity so that the inefficiency created by duplication is avoided. An unregulated vertically integrated monopolist can restrict the entry of any new entrant in the competition by refusing the bottleneck infrastructure. It has been seen that industries which are based on creating physical infrastructure has a natural monopoly because of economies of scale which persists mostly in physical infrastructure in operations and network connections\(^4\).

- **Economies of scope on supply side**- a dominant firm in a market for a network product gains benefits by being active in the complementary markets. Vertical integration can also lead to increase in moral hazard problem because these reasons are important for information goods.

- **Economies of scale on demand side**- if network externalities are not internalized, private incentives may be insufficient to sustain the new technology and adoption will be too slow. Concept of network externality from direct and indirect effects on demand side. NETWORK EXTERNALITY comes when utility of users of that network system increases with increase in number of people using the same or substitute good increases. INDIRECT NETWORK EXTERNALITY- this type of externality arises more in an industry which is dynamic in nature. For example; if I am buying a phone and one more person is buying the same phone then his consumption is not affecting me but because of buying of the same phone raises demand for that good so more firms will start making the goods with various innovations. Entry of more firms in that particular industry will increase because of the increase in demand of that particular good.

- **DIRECT NETWORK EXTERNALITY**-this type of externality arises when value of network increases as the number of subscribers increases. For example: in telecommunication if a Telephone network has \(p\) subscribers provides each subscriber with \(p (p-1)\) potential connections. Adding an additional subscriber generates \((p+1) p\) potential connections.

- Hence, adding a subscriber provides a marginal benefit of \(2p\) new connections, so the marginal benefit grows with the size of the network. Most of the cost of building and operating the network is fixed, so the marginal cost of providing network services are generally small. So this clearly indicates

\(^3\)http://www.stern.nyu.edu/networks/94-24.pdf
that expansion in the as the network increases in size, will reduce the average cost of providing the network.

->Network size leads to competitive advantages for some firms and there is a possibility that differentiated network products also exist in the market which can lead to increase in market competition.  

->If we implement full compatibility forcefully then it will give rise to free riding problem. Small firms will free ride on the investment made by the large firms which will reduce their incentive to develop and incentive.

MACRO PERSPECTIVE: NETWORK ECONOMICS AND MARKET STRUCTURE

->PERFECT COMPETITION-if network externalities are present in the economy, it is evident that perfect competition will be inefficient. Under Perfect Competition marginal social benefit (MSB) which we accrue because of network expansion will be larger than the benefit that accrues to a particular firm. Thus we can clearly say that in Perfect Competition networks are relatively smaller then the socially desired level, and in some cases they don’t provide goods even though it is socially optimal to do that because of relatively high marginal cost under Perfect Competition.

MONOPOLY

In case of monopoly that discriminates consumers on the basis of price will prefer a small network in comparison to Perfect Competition so that he can charge higher prices. Monopolist takes advantage of their position to influence the market because they know that they can influence consumer's expectation. While under the case of Perfect Competition they can’t influence the expectation. Ethically they should produce more output to meet the demand but generally they under produce so that price rises in the economy. So consumer welfare is lower in monopoly. We cannot favour monopoly structure because of existence of network externalities.

OLIGOPOLISTIC AND MONOPOLISTIC COMPETITION

In framing oligopolistic model firms assumes output as given and sets the expectation of consumers of his product. One of the issues in network economics is oligopoly under incompatible goods. Profits of the firm will increase if the costs of achieving compatibility are lower in the Industry and then the socially optimal and beneficial situation will be compatibility in the industry.

NETWORK ECONOMICS AND INDUSTRY STRUCTURE:

->INVITATION FOR ENTRY-under this structure there are two effects competitive effect and network effect. Under competitive effect competition rises as increase in number of firms operating in an industry. In network effect because of high expected sales willingness to pay and market price both increases. If network externality is strong enough then network effect will be stronger then competitive effect and because of this monopolist will invite the entrant in the market so as to increase the production.

->INTERCONNECTION BY LOCAL MONOPOLIST- in many cases it has been seen that one firm has a monopoly over a link and that link is a natural monopoly (for example in small countries like New Zealand, electricity transmission is a natural monopoly due to large fixed costs and a small market}

4 http://en.wikipedia.org/wiki/Network_economics
5 About information goods and the relevance of network economics, see Shapiro and Varian (1999).
size) and the firm who owns that natural monopoly can restrict any firm from using it. If two firms merge together then they can easily foreclose their opponent by charging significantly high price for that link. It might be feasible for the monopolist but it is not socially optimal for the monopolist.

In the market there is an indicator to judge the amount of competition in the industry. The **Herfindahl–Hirschman Index** or **HHI**. It is a measure of market share of each firm in relation to industry. It is an economic concept widely applied in competition law, antitrust and also technology management. Increase in The Herfindahl–Hirschman Index represents reduction in competition in the market and an increase in market power and vice versa. Major benefit that we can derive from this measure is that we get concentration ratios (this ratio basically represents that how much output is produced by a given number of firms in a particular industry) and this ratio provides larger weights to larger firms in comparison to small ones which shows the extent of market power of large industry and degree of oligopoly. It can range from 0 to 1.0, moving from a huge number of very small firms to a single monopolistic producer. The following formula shows the HHI

\[ H = \sum_{i=1}^{N} m_i^2 \]

\( m_i \) represents market share of firm i in the market, and \( N \) is the number of firms.

Market share directly impacts the competition incentives of the firm. A firm with a large market is able to expand its output with minimum average cost in comparison to small firms so a firm with large market share enjoys low cost and attractive products.

If we are analysing the merger between an incumbent and potential entrant then it can arise some significant competition issues in the market. If the incumbent has a larger share in the market then potential entrant will automatically get the advantage over other firms because of the reduction in start-up cost and the entrant can enjoy the benefit of the reputation of the incumbent.

**PROBLEMS WITH THIS INDEX:**

- Typical problem in defining the market is choosing a geographic scope. For example, firms may have 20% market share each, but may occupy five areas of the country in which they are monopoly providers and thus do not compete against each other. A service provider or manufacturer in one city is not necessarily substitutable with a service provider or manufacturer in another city, depending on the importance of being local for the business—for example, telemarketing services are rather global in scope, while shoe repair services are local.

- For example, if the statistic were to look at a hypothetical financial services industry as a whole, and found that it contained 6 main firms with 15% market share apiece, then the industry would look non-monopolistic. However, one of those firms handles 90% of the checking and savings accounts and physical branches (and overcharges for them because of its monopoly), and the others primarily do commercial banking and investments. In this scenario, people would be suffering due to market dominance by one firm; the market is not properly defined because checking accounts are not substitutable with commercial and investment banking. The problems of defining a market work the other way as well. To take another example, one cinema may have 90% of the movie market, but if movie theatres compete against video stores, pubs and nightclubs then people are less likely to be suffering due to market dominance.\(^6\)

\(^6\)http://en.wikipedia.org/wiki/Herfindahl_index
CHAPTER-4

TYPES OF MERGER:5a

Merger is a combination of two or more companies into one company. In India, mergers are called as amalgamations, in legal terms. The acquiring company, (also referred to as the amalgamated company or the merged company) acquires the assets and liabilities of the target company (or amalgamating company). Typically, shareholders of the amalgamating company get shares of the amalgamated company in exchange for their existing shares in the target company. Merger may involve absorption or consolidation.

-> Merger and amalgamation: the term merger or amalgamation refers to a combination of two or more corporate entity into a single entity. Forms of merger that can happen
a) absorption- one bank acquires the other.
b) consolidation- two or more banks combine to former a new entity. In India the legal term for merger is amalgamation.

Other ways of classifying merger is upon the basis of what type of corporate combine. It can be of following types-

1) Vertical merger5b: This is the merger of the corporate engaged in various stages of production in an industry. A vertical merger (entities with different product profiles) may help in optimal achievement of profit efficiency. Consolidation through vertical merger would facilitate convergence of commercial banking, insurance and investment banking. E.g : a mobile producing company merge with the company which provides them parts of mobile and software.

2) Horizontal merger5c: This is the merger of the corporate engaged in the same kind of business. E.g.: Merger of bank with another bank.

3) Conglomerate merger5d: A conglomerate merger arises when two or more firms in different markets producing unrelated goods join together to form a single firm. An example of a conglomerate merger is that between an athletic shoe company and a soft drink company. The firms are not competitors producing similar products (which would make it a horizontal merger) nor do they have an input-output relation (which would make it a vertical merger)

4) > Acquisition5e: This may be defined as an act of acquiring effective control by one corporate over the assets or management of the other corporate without any combination of both of them. Case of oracle major software firm has agreed to acquire a majority stake in Indian banking software company I-flex Solutions.
   It can be characterized in terms of the following:
   a) The corporate remain independent.
   b) They have a separate legal entity.

--> Take over:5f Under the monopolies and restrictive trade practices act, take over means acquisition of not less than 25% of voting powers in a corporate.7

5a www.icwai.org/icwai/knowledgebank/fm34.pdf
5b http://law.jrank.org/pages/8543/Mergers-Acquisitions-Types-Mergers.html
REASONS FOR MERGER:

1) Merger of weak banks- Practice of merger of weak banks with strong banks was going on in order to provide stability to weak banks but Narsimhan committee opposed this practice. Mergers can diversify risk management.

2) Increase in market competition- Innovation of new financial products and consolidation of regional financial system are the reasons for merger.9

3) Markets developed and became more competitive and because of this market share of all individual firm reduced so mergers and acquisition started.

4) Capability of generating economies of scale when firms are merged.

5) Transfer of skill takes place between two organisation takes place which helps them to improve and become more competitive.

6) Globalisation of economy impacted bank mergers.

7) New services and products- Introduction of e- banking and some financial instruments / derivatives.

8) Technology- Removal of entry barrier opened the gate for new banks with high technology and old banks can’t compete with them so they decide to merge.10

9) Positive synergies- When two firms merge their sole motive are to create a positive effect which is higher than the combined effect of two individual firms working alone. Two aspects of it are cost synergy and revenue synergy.

Cost Synergy is the savings in operating costs expected after two companies that complement each other's strengths join. Revenue Synergy is refers to the opportunity of a combined corporate entity to generate more revenue than its two predecessors stand-alone companies would be able to generate.

IMPACTS OF MERGER:

1) Diversification- When two firms merge their risk in investing assets diversify accordingly. When a firm is operating alone then they don’t have many options to diversify their portfolio investment that they can get after merger.

2) Mergers and Acquisition allows firms to obtain efficiency gains through cost reductions(cost synergies) , revenue increases( revenue synergies)

3) Broader array of products- When two firms merge they have diversified variety of products and after the merger each consumer in both the firms will be benefited with the range of products or services to choose from.

5cIbid
5dhttp://www.wisegeek.com/what-is-a-conglomerate-merger.htm
5ewww.investorwords.com/80/acquisition.html
5fwww.investorwords.com/4868/takeover.html
9http://law.jrank.org/pages/8543/Mergers-Acquisitions-Types-Mergers.html
10http://www.learnmergers.com
4) Mergers and Acquisition helps firms to widen its consumer portfolio but it also leads to a more diversified range of services and offer scope economies by optimizing the synergies between the merged activities.

5) Domestic mergers cut costs for both the partners whereas for the majority of cases including domestic and cross border mergers and acquisition, the impact on profitability is insignificant but a clear trend to diversify the sources of revenue was apparent.

6) In terms of cost efficiency and revenue efficiency it has been noticed that in domestic merger organisation get the benefit of cost efficiency (reduction in operating cost) and in cross border merger organisation get the benefit of revenue efficiency (increase in revenue) because of the benefit of geographical expansion and diversification.

7) Improvement in the activities of organisation, however, offer benefits from product complementarities which helps to enhance revenues.

8) Efficiency may be improved after merger and acquisition, if the acquiring company is more efficient already and brings the efficiency of the target up to its own level by providing its managerial expertise, policies and other operations.
### HISTORY OF BANKING MERGERS IN EUROPEAN UNION:

Some of the important bank mergers of Europe:

- In the year 1997, Union Bank of Switzerland merged with Swiss Bank.
- In 1998, Banque Nationale de Paris (BNP) of France went through a merger with Banque Paribas and a new bank was formed with market capital of $688 billion.
- In the same year of 1998, the merger between Hypobank and Bayerische Vereinsbank, created a new banking institution which became the second largest bank in Germany.
- In 1999, Banco Santander acquired Banco Central Hispano and became the largest bank in Spain.
- In the same year of 1999, Bank Austria did a merger deal with Creditanstalt Bankverein and became the largest bank in Austria.
- In the same year of 2000, Credit Suisse of Europe acquired Donaldson, Lufkin and Jenrette.
- Recently, in 2007, two Italian Banks, UniCredit and Capitalia merged and became the second largest bank in Europe after HSBC.

### MAJOR BANKING MERGER IN US

<table>
<thead>
<tr>
<th>YEAR OF MERGER CLOSED</th>
<th>TARGET COMPANY</th>
<th>ACQUIRING COMPANY</th>
<th>NAME OF THE MERGED IDENTITY</th>
<th>ULTIMATE SUCCESSOR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1930</td>
<td>Chase National Bank</td>
<td>Equitable Trust Co of NY</td>
<td>Chase National Bank</td>
<td>JP Morgan Chase &amp; Co</td>
</tr>
<tr>
<td>1941</td>
<td>Berks county trust company</td>
<td>Union national bank</td>
<td>Berks county trust company</td>
<td>Wells Fargo</td>
</tr>
<tr>
<td>1948</td>
<td>Chemical bank &amp;trust co</td>
<td>Continental bank &amp; trust co of NY</td>
<td>Chemical bank &amp;trust co</td>
<td>JP Morgan Chase and co</td>
</tr>
<tr>
<td>1951</td>
<td>National city bank of New York</td>
<td>First National city bank of New York</td>
<td>First national city bank</td>
<td>Citigroup</td>
</tr>
<tr>
<td>1955</td>
<td>Bankers trust</td>
<td>Public national &amp; trust co</td>
<td>Bankers Trust</td>
<td>Deutsche</td>
</tr>
<tr>
<td>1957</td>
<td>Commercial national bank</td>
<td>American trust &amp; co</td>
<td>American commercial bank</td>
<td>Bank of America</td>
</tr>
<tr>
<td>1975</td>
<td>Chemical bank New York bank &amp; co</td>
<td>Security national bank</td>
<td>Chemical bank New York bank &amp; co</td>
<td>JP Morgan Chase &amp; co</td>
</tr>
<tr>
<td>Year</td>
<td>Acquirer</td>
<td>Acquired</td>
<td>Event Description</td>
<td></td>
</tr>
<tr>
<td>------</td>
<td>------------------------------</td>
<td>----------------------------------------</td>
<td>-----------------------------------------------------------------------------------------------------------------------------------------------------</td>
<td></td>
</tr>
<tr>
<td>1983</td>
<td>Bank America corp.</td>
<td>Seafirst bank</td>
<td>Bank America corp. requested to acquire Seafirst bank. Bank of America paid $2.43 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>1987</td>
<td>Fidelity bank</td>
<td>First fidelity bank</td>
<td>Investment by competition commission stated that Merrill Lynch reported a profit of $2.1 billion for second quarter of 2007. Suddenly in third quarter profit turned into losses due to the bad accounting practices by Merrill Lynch. Company was not reporting the actual values of its bad investment. As Merrill Lynch’s unethical practices were revealed, it was forced to ultimately report its real financial position.</td>
<td></td>
</tr>
<tr>
<td>1991</td>
<td>NBD bank corp.</td>
<td>Summcorp.</td>
<td>Union bank requested to acquire Summcorp. NBD bank paid $2.2 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td>Union bank</td>
<td>Bank of California</td>
<td>Bank of Americacorp. requested to acquire Union bank. Union bank of NA paid $2.1 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>Travellers group</td>
<td>Citicorp</td>
<td>Citigroup requested to acquire Travellers group. Citigroup paid $1.9 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>Bank of America</td>
<td>Merrill Lynch</td>
<td>Bank of Americacorp. requested to acquire Merrill Lynch. Bank of America paid $1.7 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>Wells Fargo</td>
<td>Wachovia</td>
<td>Wells Fargo requested to acquire Wells Fargo. Wells Fargo paid $1.6 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>PNC financial services</td>
<td>National city corp.</td>
<td>PNC financial services requested to acquire National city corp. PNC financial services paid $1.5 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td>PNC financial services</td>
<td>RBC Bank</td>
<td>PNC financial services requested to acquire RBC Bank. PNC financial services paid $1.4 billion to shareholders who claimed that bank made false statement about company’s health.</td>
<td></td>
</tr>
</tbody>
</table>

**COMPETITION ISSUES IN Mergers AND Acquisition IN US AND European Union**

**Major Acquisition that Took Place in Past Years:**

**BANK OF AMERICA ACQUIRED MERRILL LYNCH:**

Bank of America, a financial holding company under the Bank Holding Company Act (BHCA), requested to acquire Merrill Lynch Inc. and its subsidiary in Istanbul, Turkey, and New York. Bank of America paid $2.43 billion to shareholders who claimed that bank made false statements about company’s health. Investigation by the competition commission stated that Merrill Lynch reported a profit of $2.1 billion for the second quarter of 2007. Suddenly in the third quarter, profit turned into losses due to the bad accounting practices by Merrill Lynch. Company was not reporting the actual values of its bad investment. As Merrill Lynch’s unethical practices were revealed, it was forced to ultimately report its real financial position.10

Bank of America board failed to perform its fiduciary duties to its shareholders in its merger with Merrill Lynch. This claim was made on the basis of the following facts:

1) Boards prioritization of retailing its position at the expense of shareholder’s value.

2) Bank of America’s failure to conduct proper due diligence prior to acquisition of Merrill Lynch.

---


3) Bank of America's failure to maintain transparency regarding Merrill Lynch's financial situation.

4) Unethical executive compensation.

5) Bank of America also did not disclose an agreement to pay $5.8 billion of bonuses to Merrill employees, in the face of huge losses at the investment bank.

**PERFORMANCE OF THE MERGED ORGANISATION:**

Bank of America Corporation (BAC) after buying Merrill Lynch posted a loss of about $2.4 billion in for the quarter ending December 2008. Bank of America also lost about $1 billion for the third quarter of 2009. For the period, BAC reported that its personnel costs and operating costs increased to $16.3 billion from $11.7 billion previous year, mainly due to Merrill Lynch acquisition. Merrill Lynch continues to be a loss making centre for BAC as mentioned BAC in its 10Q of Q3 09 -“net loss increased as higher gains on the sale of debt securities and higher equity investment income were more than offset by the negative credit valuation.

⇒ **ACQUISITION OF FORTIS BELGIAN AND LUXEMBOURG ASSETS BY BNP Paribas:**

BNP Paribas is present in Belgium and Luxembourg in credit cards through its subsidiary PFB, which issues cards under the Master card label and Aurora brand. The Commission's concerns centred on credit cards as a payment instrument as well as on the provision by the Parties of credit to consumers through the cards. The Commission's concerns do not relate to the acquiring side of the market. The Commission's investigation indicated that in Belgium the merged entity would have become by far the largest player in card issuing and the related provision of credit, and that the concentration, as initially notified, would have reduced choice in the market, both from the standpoint of commercial partners involved in distribution and co-branding arrangements with card issuers and from the viewpoint of the final cardholder. Further clearance was granted if BNPP's divestment of BNP's Belgian consumer card subsidiary. Divestment would substantially offset the increase in market share due to the merger on the problematic markets and would maintain robust competition to the benefit of the number of market in which the overlap of the parties was limited.  

12  

BANCA ANTONVENETA (BA) ACQUIRED BY DUTCH ABN AMRO AND BANCA NAZIONALE DE LAVORO ACQUIRED BY BANCO BILBAO VIZCAYA ARGENTINA (BBVA)

These two cases are from Italy and both the deals were earlier blocked by competition commission in Italy and Government of Italy. Although acquisition of Banca Antonveneta (BA) was later approved but merger review process was delayed and it increased uncertainty and risk for ABN Amro. Second deal failed after Banco Bilbao Vizcaya Argentina (BBVA) withdrew its takeover bid in response to a counterbid by Italian insurer Unipol for BWL. Deals were blocked to protect local banks from foreign investors, EU commission brought actions against Italy for infringement of the principle of the free movement of capital and freedom of establishment. Merger control is not only a barrier to cross border consolidation in Europe but it constitutes a systematic barrier to cross border consolidation in Europe. Regulators also blocks cross border mergers and acquisition. Refusal of Acquisition of Banca Antonveneta was vetoed by the Portuguese government.

**GROUNDS OF REFUSAL:**

- Late and incomplete notification.
- Absence of a transparent and complete structure.
- Necessity to protect national interest.

PNC FINANCIAL SERVICES MERGER WITH NATIONAL CITY BANK:

PNC, with total consolidated asset is about $145.6 billion, which is the 14th largest depository organisation in US. National City with total consolidated assets of approximately $143.7 billion is the 16th largest depository organisation in US. On fulfilment of this proposal and considering all the uncertainty, PNC would become the eighth largest depository organisation in US. PNC would control total assets of about $174.8 billion. In Ohio it will become the largest depository organisation. The BHC Act (bank holding company act) has to investigate some of the competition issues in this merger.

- To reduce potential adverse effects on competition in the Pittsburgh market PNC has proposed to divest 50 of National city bank branches that accounts for $3.5billion deposits.

- PNC proposed to merge with second big depository organisation (in some areas) and all other competitor have relatively smaller market share in those areas. Review took time because size of those institutions relative to other market competitor.

- In conducive analysis board generally don’t adjust market deposits to exclude specific types of deposits. But in this case it was advice to do that.
UNICREDIT AND CAPITALIA MERGER:

ANTITRUST AUTHORITY GIVES CONDITIONAL GO-AHEAD TO UNICREDIT-CAPITALIA MERGER

At its meeting on 18 September 2007, the Italian Competition Authority decided to authorize the takeover of Capitalia by Unicredit under strict conditions. The Authority’s authorization also took into account the beneficial effects which will accrue from it to consumers in terms of significant cost reductions and improvements in the quality of service.

Conditions for merger proposed by competition commission were as follows:

->The new bank must sell between 155 and 180 branches in 16 Italian provinces to independent third parties who are not shareholders in the new bank.

->In 8,000 branches of competing banks in approximately 4,000 municipalities in Italy where the UCI Group will not have ATMs, customers of the new bank will not have to pay a commission for Bancomat cash withdrawals; such commissions will also be significantly reduced in the rest of the country. Commissions are also to be eliminated for withdrawals made abroad.

->The new bank must sell its shares in Generali and 9.39% of its holding in Mediobanca must be disposed of according to strict rules. The remaining 8.68% may not be increased in any way.

->Restrictions on Board members of the new bank who hold positions in Mediobanca or Generali: they must abstain from voting on investment banking and insurance matters.

->The remaining block of 8.68% to be held by the future entity is also frozen. In the run-up to the sale, UniCredit may not exercise its relevant voting rights under the block voting agreement or in Mediobanca meetings.

MEASURES RELATING TO CONFLICTING ROLES

Members of UCI’s Board holding positions in the governance of Mediobanca or Generali may not take part in discussions or voting on resolutions by the Board of the new bank having to do with the investment banking or insurance markets in Italy. Internal organizational measures must be adopted to ensure that such directors do not receive sensitive information. This measure will prevent parties simultaneously present on the Boards of UCI and Mediobanca having access to a set of information and decision-making powers that may condition those companies’ strategic choices in an anti-competitive manner.

MAIN FINDINGS OF THE MERGERS AND ACQUISITIONS IN US AND EU

-> TRANSPARENCY-during mergers banks should maintain transparency with their shareholders, employees and government. As we have seen that during merger of Merrill Lynch and Bank of America transparency was not maintained with the shareholders. Banks should not merge on the expense of shareholders value. Lack of due diligence can create problems in future. When shareholders owns shares in a bank/company they become owner of the company up to the amount they have invested so they have all the right to know about the merger details and the financial condition of the target bank they are planning to own.

-> Commission generally don't restrict the merger on the basis of number of deposits held by the bank or number of branches banks have but in some special cases commission can do that if it raises competition issue.

-> Sometimes commission objects the merger in order to keep the nations interest. This type of restriction has been noticed in cross border merger where merger of any bank with a big player can eliminate local banks.

-> When two big players merge together then to reduce the potential adverse effect on competition because of low market share of bank in a particular area commission notify the big players to reduce the number of shares and deposits held by them.

-> In some cases commission's concern do not relate to acquiring side of the market. Mergers in the problematic area can be offset by divestment and competition can be done fairly.

-> In most of the cases discussed above got permission for merger under special circumstances and under certain conditions.
### MERGERS AND ACQUISITION EXPERIENCE OF INDIA

#### BANK MERGERS IN THE POST REFORM PERIOD:

<table>
<thead>
<tr>
<th>Merger year</th>
<th>Target bank</th>
<th>Acquirer</th>
<th>Motive</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>New bank of India</td>
<td>Punjab National bank</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1994</td>
<td>Bank of Karad Ltd</td>
<td>Bank of India</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1995</td>
<td>Kashinath Seth bank</td>
<td>State bank of India</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1996</td>
<td>Punjab co-op Ltd</td>
<td>Oriental bank of commerce</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1997</td>
<td>Bari Doab bank Ltd</td>
<td>Oriental bank of Commerce</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1999</td>
<td>Bareilly coop Ltd</td>
<td>Bank of Baroda</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>1999</td>
<td>Sikkim bank Ltd</td>
<td>Union Bank of India</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2000</td>
<td>Times bank Ltd</td>
<td>HDFC Bank Ltd</td>
<td>Voluntary merger</td>
</tr>
<tr>
<td>2001</td>
<td>Bank of Madura</td>
<td>ICICI Bank</td>
<td>Voluntary merger</td>
</tr>
<tr>
<td>2002</td>
<td>ICICI Ltd</td>
<td>ICICI Bank</td>
<td>Universal banking objective-merger of financial institution with bank</td>
</tr>
<tr>
<td>2002</td>
<td>Banaras State bank Ltd</td>
<td>Bank of Baroda</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2003</td>
<td>Nedungadi Bank Ltd</td>
<td>Punjab National Bank</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2004</td>
<td>IDBI Bank Ltd</td>
<td>Industrial development bank of India</td>
<td>Universal banking objective-merger of financial institution with bank</td>
</tr>
<tr>
<td>2004</td>
<td>South Gujarat local area bank</td>
<td>Bank of Baroda</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2004</td>
<td>Global trust bank</td>
<td>Oriental bank of commerce</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>Year</td>
<td>Bank 1</td>
<td>Bank 2</td>
<td>Reason</td>
</tr>
<tr>
<td>------</td>
<td>-------------------------</td>
<td>-------------------------</td>
<td>-----------------------------</td>
</tr>
<tr>
<td>2005</td>
<td>Centurion bank</td>
<td>Bank of Punjab</td>
<td>Voluntary merger</td>
</tr>
<tr>
<td>2006</td>
<td>Ganesh bank of Kurandwad</td>
<td>Federal bank</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2006</td>
<td>United western bank</td>
<td>Industrial development bank of India</td>
<td>Forced merger-restructuring of weak bank</td>
</tr>
<tr>
<td>2006</td>
<td>Lord Krishna bank</td>
<td>Centurion bank of Punjab</td>
<td>Expansion of size-voluntary merger</td>
</tr>
<tr>
<td>2006</td>
<td>Sangli bank</td>
<td>ICICI bank</td>
<td>Voluntary merger</td>
</tr>
<tr>
<td>2007</td>
<td>Bharat overseas bank</td>
<td>Indian overseas bank</td>
<td>Regulatory intervention</td>
</tr>
</tbody>
</table>

**RECENT Mergers AND Acquisition NEWS IN INDIA:**

The Indian banking industry may see a few mergers and acquisitions (M&A) deals this year, ahead of the banking regulator releasing the licensing norms for new banks that are expected to open for business in the next two years.

At least three new generation private sector banks—HDFC Bank Ltd, Kotak Mahindra Bank Ltd and IndusInd Bank Ltd have set their eyes on acquisitions.

**Kotak Mahindra Bank** has already created a war chest for acquisitions by selling 4.5% stake in the bank for $296 million (around Rs1, 400 crore today) to Sumitomo Mitsui Financial Group Inc. Its vice-chairman and managing director Uday Kotak has previously said that he is "sniffing around" for acquisitions.

**ICICI Bank Ltd**, India’s largest private sector lender, is in the process of acquiring Bank of Rajasthan Ltd for its 463 branches. ICICI Bank had earlier acquired Bank of Madura Ltd and Sangli Bank Ltd, again for their branches, and their presence in southern and western India, respectively.

**Yes Bank** Ltd is in talks to buy the local retail and commercial operations of Royal Bank of Scotland Group (RBS). A plan by RBS, majority owned by the UK government, to sell the Indian businesses to HSBC Holdings fell through in November last year, more than two years after the two banks started negotiations. Yes Bank, India’s No. 4 private sector lender with assets of nearly $11 billion, is likely to start due diligence on the RBS unit soon. RBS has been shrinking its Indian business since the original deal with HSBC was struck in 2010 and it now has assets of just 190 million pounds. The unit has 31 branches, 400,000 customers and made revenue of 42 million pounds in the first nine months of last year, RBS said in a statement last November.

**CURRENT SCENARIO OF INDIAN BANKS:**

The total assets of Indian banks, which are regulated by the Reserve Bank of India (RBI) and the Ministry of Finance (MoF) 1, were pegged at Rs 82,99,220 crore (US$ 1564.8 billion) during FY122
Source: ICRA, Thomas White Report on Indian Banking

AFTER MERGER SCENARIO (HERE WE MERGERD ALL SUBSIDIARIES OF STATE BANK OF INDIA)
WHY THERE IS A NEED FOR CONSOLIDATION OF INDIAN BANKS:

Financial Sector Reforms set in motion in 1991 have greatly changed the face of Indian Banking. The banking industry has moved gradually from a regulated environment to a deregulated market economy. Banks in India are gradually moving towards
1) Consolidation of players through mergers and acquisitions,
2) Globalization of operations,
3) Development of new technology and
4) Universalization of banking.

- As we are entering into an international banking phase it is must to have a fair number of large banks, which could play a meaningful role in the emerging economics. International banking system is dominated by large players.

- The factors including mergers and acquisitions usually include technological progress, excess capacity, emerging opportunities, consolidation of international banking markets and deregulations of geographic, functional and product restrictions. Policy inducements such as the government’s incentives that could accrue to the top managers are also other important factors, which may determine the pace of consolidation.

- The major gains perceived from bank consolidation are the ability to withstand the pressures of emerging global competition, to strengthen the performance of the banks, to effectively absorb the new technologies and demand for sophisticated products and services, to arrange funding for major development products in the realm of infrastructure, telecommunication, etc. which require huge financial outlays and to streamline human resources functions and skills in tune with the emerging competitive environment.

- The international experience reveals a wide range of processes and practices involving consolidation, their impact on the banking market and the trends in post-merger performance of banking institutions. These experiences could provide useful inputs to the banking policy in India.

- An important observation which may be induced from various past mergers that the merger between big and small banks led to greater gains as compared to merger between equals. It is also observed from past experiences that if the merger follows business aided by appropriated technology and diversified product range, it could lead to greater gains for the banking industry as a whole. Similarly, consolidation increases the market power and does not cause any damage to the availability of services to small customers.

- Indian banks have unique character in displaying similar characteristics of performance despite consisting of different size and ownership. This trend further substantiates the scope for consolidation across banks group.
CHAPTER-7

HYPOTHETICAL SITUATION:

Five major public sector banks in India are State bank of India, Punjab National bank, Bank of Baroda, Canara bank and Bank of India.

State Bank of India (SBI) is a multinational banking and financial services company based in India. It is a government-owned corporation with its headquarters in Mumbai, Maharashtra. As of December 2012, it had assets of US$501 billion and 15,003 branches, including 157 foreign offices, making it the largest banking and financial services company in India by assets. SBI has 20% market share in deposits and loans among Indian commercial banks. SBI has a number of associate banks in different parts of the country. In the past few years, it has been merging some of these subsidiaries such as State Bank of Indore and State Bank of Saurashtra with itself in the past three years. Three other associates are listed such as State Bank of Bikaner & Jaipur, State Bank of Travancore where it holds 75% and State Bank of Mysore, where it holds 92%. In the remaining two banks - State Bank of Hyderabad and State Bank of Patiala SBI holds 100% stake.

Punjab National Bank (PNB) is an Indian financial services company based in New Delhi, India. PNB is the third largest bank in India by assets. PNB is currently the second largest state-owned commercial bank in India with about 5000 branches across 764 cities. It serves over 37 million customers. The bank has been ranked 248th biggest bank in the world by the Bankers' Almanac. The bank's total assets for financial year 2007 were about US$60 billion. PNB has a banking subsidiary in the UK, as well as branches in Hong Kong, Dubai and Kabul, and representative offices in Almaty, Dubai, Oslo, and Shanghai.

Bank of Baroda (BoB) is an Indian state-owned banking and financial services company headquartered in Vadodara. It offers a range of banking products and financial services to corporate and retail customers through its branches and through its specialised subsidiaries and affiliates in the areas of retail banking, investment banking, credit cards and asset management. Its total global business was ₹8,021 billion as of 31 mar 2013.

Canara Bank is an Indian bank headquartered in Bangalore, Karnataka. It was established in 1906, making it one of the oldest banks in the country. As of December 2011, the bank had a network of 3564 branches and 4000 ATMs spread across India. The bank also has offices abroad in London, Hong Kong, Moscow, Shanghai, Doha, and Dubai. Widely known for customer centricity. The bank was nationalised in 1969. As at March 31, 2002, Canara Bank had a market share of 5.32 per cent of total deposits and 5.13 per cent of total advances of all scheduled commercial banks (SCBs). Canara Bank's rating reflects its strong market position, adequate capitalisation levels, and comfortable liquidity profile. The rating also factors the bank's business profile that is supported by a good resources position, as well as its better asset quality as compared to its peers.

Bank of India (BoI) is an Indian state-owned commercial bank with headquarters in Mumbai, Maharashtra. Government-owned since nationalisation in 1969, it is India's 4th largest PSU bank, after State Bank of India, Punjab National Bank and Bank of Baroda. It has 4187 branches as on 21
April 2012, including 52 branches outside India, and about 1679 ATMs. Bank of India is a founder member of SWIFT (Society for Worldwide Inter Bank Financial Telecommunications), which facilitates provision of cost-effective financial processing and communication services. The Bank completed its first one hundred years of operations on 7 September 2006.

**Question arises that if these five (SBI, PNB, CANARA BANK, BANK of INDIA, And BANK OF BARODA) major Public sector banks merge together what will be the impact on competition and the economy.**

Whether or not these mergers are socially beneficial on average, there may be identifiable circumstances that may help guide the policy decisions about individual mergers. Current antitrust policy relies heavily on the use of the ex-ante Herfindahl index of concentration for predicting market power problems and considers operating efficiency only under limited circumstances.

Mergers and acquisitions could raise profits in any of three major ways. First, they could improve cost efficiency, reducing costs per unit of output for a given set of output quantities and input prices. Indeed, consultants and managers have often justified large mergers on the basis of expected cost efficiency gains.

Second, mergers may increase profits superior combinations of inputs and outputs. Through improvements in profit efficiency that involves Profit efficiency is a more inclusive concept than cost efficiency, because it takes into account the cost and which is taken as given in the measurement of cost revenue effects of the choice of the output vector, efficiency. Thus, a merger could improve profit efficiency without improving cost efficiency if the reconfiguration of outputs associated with the merger. Third, mergers may improve profits through the exercise of additional market Power in setting prices. An increase in market concentration or market share may allow the consolidated firm to charge higher rates for the goods or services it produces, raising profits by extracting more surplus from consumers, without any improvement in efficiency. See U.S. Department of Justice and Federal Trade Commission (1992).

According to the study conducted by US it has been seen that borrowers lose on average about 0.8% in equity value when an announcement identifies their bank as a merger target. Small borrowers of target banks are especially hurt. As we can see from the data of market share that if we merge top five public sector banks then more than 39% share out of whole 75% share corresponding to government banks will go in the hands of these banks which can arise competition issues in banking sector.

Post-merger increase product switching may indicate reduced customer satisfaction or that merged firms effectively drive out customers. Sapienza (2002) finds that exit rates for borrowers of target banks increase after a bank merger, and suggests that management of newly merged banks effectively kicks out small borrowers.

Small firms may also be very sensitive to changes in market power resulting from bank mergers since they are unlikely to have many sources of finance like large banks. In the past studies it has been noticed that when banks with such a large share merge together then operating cost reduces because doubling of activities reduces.

---

The banking industry has relatively clean, detailed data available from regulatory reports that give information on relatively homogeneous products in different local markets with various markets. Complexity will also become greater as financial services industries evolve, as financial markets and products become more complex and global.

Instability relates to bank risk-taking on the asset side. Because of their substantial financing from many small, relatively uninformed depositors and an often-existing public safety net in response to the previously mentioned vulnerability, banks can be prone to taking on 'excessive' risk in the choice of which projects to finance.

It has been noted that after merger they get more access to new markets because of the fact that some banks have access in remote areas which other banks don't have so after merger the acquiring bank also gets the access to these areas. If merging banks have significant geographical overlap in their markets of operation, mergers can lead to an increase in market power, which would in turn increase the cost of capital for borrowers. After the merger of banks who contains most of the market share then access to these remote place will increase and bank will better understand the needs of the people in remote areas.

The report attributes much of the foundering of M&A expectations to shortcomings in dealing with the human resource fallout of redundancies, which may seriously undermine operational capabilities and employee morale. Among the consequences of heightened merger activity for the financial sector workforce that survives the restructuring, the report cites "reduced job security, increased workloads, anxiety and stress," all of which can impinge negatively on performance in an intensely competitive work climate. The report cites, conservative estimates indicating that at least 130,000 finance jobs have disappeared in western Europe as a result of M&As during the 1990s and there are predictions of "the disappearance of approximately 300,000 banking jobs between 1999 and 2002 through merged consolidation. British banks, for a variety of reasons including M&As, "reduced their employees by 150,000 and shut a quarter of their total network of branches" between 1990 and 2000.

In the United States, the number of commercial banks dropped by 30 per cent over the decade up to 1995, while employment levels declined by about 5 per cent between 1984 and 1994. The acquisition of Bank of America by Nations Bank in 1998 included plans to lay off 18,000 workers by 2002. 1999 merger between BNP and Paribas, that the combined bank would shed 5,700 posts, including some 3,600 in France.

The inevitable decline in sectorial competition and service that results from greater concentration in the financial industry, leading to reduced credit support to small-and medium-sized enterprises, which are the major generators of employment in all economies.

Bank mergers will increase or decrease loan spreads, depending on whether the increased market power outweighs gains in operating efficiency. This is consistent with the theory of merger that large banks rely heavily on hard information and, consequently, lend mostly to large and transparent borrowers while small banks better utilize soft information and specialize in lending to small and opaque borrowers.
Some banks joined in the merger at their hard economic times (Bank of America and Merrill Lynch) and survived collapse since they were able to acquire operating capital from the other members in the merger. Therefore, financial benefit for the individual firms and desires to access global market was the initial driving forces to joining the merger.

The major benefit accrued from this consolidation is the reduction of charges to costumers due to the stiff competition facing the industry thus making them offer better rates. This has been made possible since the mega-banks enjoy high economies of scale and therefore are capable of offering relatively low rates compared to other small banks. The small banks are left to try strengthening their costumer relation system to maintain their clients since they cannot out do the mergers in the monetary competition. The shareholders of the mergers are also assured more benefits due to the greater income associated with the mergers and therefore are even enticed to invest more into the business.

A rise in operating risk might also occur if top management is less able to supervise its employees directly because of an increase in size (before Merrill Lynch Bank of America acquired Fleet Boston, MBNA, Losalle bank, and Countrywide) which later resulted as a collapse of management and after that Nations bank acquired Bank of America.

An expansion in the range of services made available to the public-In the studies of US merger during period 1980-1990, the consolidation process has brought in more competition, thus resulting in delivery of innovative financial products with more efficiency and more variety. This includes availability of specialized electronic systems which could be otherwise exorbitant to be acquired by single banks. After merger every bank learns something from each other and this learning process help them to grow in the competition. Merger of Citicorp and Travelers group was held because of the fact that Travellers group had client base of investors and insurance customers. They provided Citi a sound market of mutual fund, investment product fir middle class and retail customers.

One more example regarding this topic was merger of BANK OF AMERICA AND MBNA- This merger bought expertise in affinity market and electronic transaction processing and provided new opportunities to cross sell each other's product. After this merger Bank of America became one of the leaders in debit card transaction.

When Bank of America acquired Losalle bank they gained a huge share in Chicago and Detroit. Additional branches and 17000 commercial clients took them ahead of JP Morgan and co.

Coordination problems raised in past -Different banks have different culture so after merger it takes a lot of time for the employees of acquired bank to change the culture and environment suddenly. It may make employees of acquired bank less efficient and demoralized. So after merger it is the duty of the acquiring banks to coordinate with them in every aspect. This issue has been noticed in the merger of PNC FINANCIAL SERVICES MERGER WITH NATIONAL CITY BANK. It has been noticed that a reverse trend happened and acquiring company provided shares of their banks to the employees of the target company and it created problem inside the system of the bank.

Diversification of portfolio- The data of US mergers shows that these are consistent with the hypothesis that megamergers tend to diversify the portfolio and reduce risk, which allows the consolidated bank to issue more loans for about the same amount of equity capital, raising profits on average. Consolidated banks try to expand their loan portfolios. Because of mergers banks get expanded geographical areas for expanding their loan portfolio and to take risk
Better pays, incentives and career opportunities for employment. Post mega mergers effects can be seen in the hire and fire system of banks. Since large banks merged together so for them hiring a new employee and firing a employee is easy. But it will provide opportunities for banks as well as the employee to improve their performance and growth.

Market concentration is a useful indicator of the likely potential competitive effect of a merger. Here as we know that to calculate market share we use **Herfindahl–Hirschman Index** or **HHI**.

In our case before merge the five big public sector banks will have

\[ (22^2+6^2+5^2+5^2+5^2) = 595 \]

Private sector banks and other banks included then HHI will come out to be

\[ 595 + 5^2+4^2+4^2+3^2+4^2 = 2425 \]

After merger of these five big public sector banks including other banks and private banks HHI index will come out to be:

\[ (22+6+5+5+5)^2 = 1849 + 42^2+5^2+4^2+3^2+3^2 = 3672 \]

General standards for mergers with competitive index are:

- A HHI index below 0.01 (or 100) indicates a highly competitive index.
- A HHI index below 0.15 (or 1,500) indicates an unconcentrated index.
- A HHI index between 0.15 to 0.25 (or 1,500 to 2,500) indicates moderate concentration.
- A HHI index above 0.25 (above 2,500) indicates high concentration.

Small index of HHI represents that there is no dominant player in the competitive market which can influence the market according to their convenience.

If we are looking at these from a particular point of view (considering HHI) then this system states that after merger of five big public sector banks, competition issue will arise because of the fact that HHI index represents that after merger the banking industry will see high concentration of market and if we consider the past experience then also we can see there is a possibility that competition issues may arise in future. So there are two aspects of looking and judging competition issues so it depends on the prevailing system that which method will work better in which conditions. Considering past experience there is a possibility that at the time of merger of two banks financial crisis or uncertainty prevailed in the market and those factors lead to failure of merger and raised competition issues.

In conclusion, note that, although the HHI is a useful tool in merger analysis, particularly as an initial screening device, other factors are considered in an economic analysis of competition\(^\text{13}\).
CONCLUSION:

Primary purpose of mergers and acquisition is to reduce competition and protect existing markets in the economy. Overall mergers and acquisitions have their own pros and cons. But mergers are good for the growth and development of country only when it does not give rise to competition issues.

Mergers improve the competition edge of the industry in order to compete in the global market but mergers shrink the industry because number of firms reduces. Mergers help banks to strengthen their financial base and access tax benefits and direct access to cash resources.

After analysing the merger trends in European Union (1990s) we can say that merger has led not only to the emergence of large banking groups but also helped in consolidating fragmented markets.

But in the recent years these trends has been changed. One striking feature which was noticed in comparison to domestic mergers and cross border mergers was that in domestic mergers if no competition issue were raised then cost will reduce because of reduction in operating cost. But in case of cross border mergers it has been noticed that revenue tends to improve without imposing negative impact on consumers. Setting of priorities in advance is beneficial for the acquiring company.

If banks have priority to reduce capacity in domestic market then further consolidation is required in domestic market. Banks should opt for cross border merger if they have managed to reach the threshold level of concentration in domestic market.

Mergers and acquisition are done for consolidating strategies in order to expand the geographical area of operation but optimal level of cooperation should be allowed and followed so as to gain proper advantage of mergers.

Too many mergers inside or outside can be harmful for the economy and leads to economic failure. From society's point of view too many mergers should be avoided. But we cannot restrict all mergers which includes at least one big player in the economy instead we should reconsider our competition policies.

CCI aimed at ensuring that banks compete among themselves in fighting for customers by offering the best terms, lower interest rates on loans and higher interest rates on deposits and securities. Merger regulation by CCI would be therefore intended to ensure that such activities are not motivated by the desire to collude and make excessive profits at the expense of customers or to squeeze other players out of the market through abusive practices.
RECOMMENDATIONS:

->ENVIRONMENT-government should provide favourable environment for domestic and cross border mergers under controlled environment and system in order to get financially strong banks with good capital base. In case of unfavourable environment growth will be restricted in any industry.

->Policies regarding mergers should be made in such a way so that it controls monopoly and anti-competitive practices in banking sector. But policies should not restrict the entry of any new firm because of the policies. Over protecting policies restrict the firm from taking risk and explore new areas which restrict the innovation process in any field.

->Commission should frame a policy which explains that there should be a minimum capital base for all banks to run the operation successfully and in a risk free environment.

->Present policies are ill framed and equipped to handle competition issues because of this we have seen so many unproductive mergers in the recent news

->We should incorporate a full efficiency test in our competition policies and it would be desirable to restructure capital markets in small and medium banks.

->We should provide proper incentives to these small and medium banks so that they start innovating with their quality of services provided to common people.

->A McKinsey report suggests that banks in India need to recruit employees with the both core and specialist skills, and control attrition especially at the junior levels. Non private Indian banks will greatly benefit from productivity improvements, such as a re-engineering of the institutions knowledge processes, better use of technology and building industry level utilities.14

->In this matter CCI should seek expert opinion on each of the proposed M&A falling in its jurisdiction. Towards this it may keep a panel of many experts in financial, Industry segments etc. This will help in quickly requisitioning the services. Panel must only contain Expert In their own capacity and not Organizations or firms which can have other business Interests. Such other checks and balances can be thought out.

14 McKinsey report – Human Capital is the Key to Unlocking a Golden Decade in Indian Banking
REFERENCES:

http://www.ibef.org/download/Banking-Sector-04jan.pdf
WWW.ibef.org
The Future of Banking” FDIC Banking Review 2004, v. 16 n. 4 page 122
online.wsj.com/public/resources/documents/RepublicanMemobofa0610.pdf

http://blogs.wsj.com/deals/2008/10/03/can-citigroup-kill-the-wells-fargo-wachovia-deal/

McKinsey report – Human Capital is the Key to Unlocking a Golden Decade in Indian Banking


http://en.wikipedia.org/wiki/Banking_in_India

http://en.wikipedia.org/wiki/Network_economics
About information goods and the relevance of network economics, see Shapiro and Varian (1999).

http://en.wikipedia.org/wiki/Herfindahl_index

http://www.msmementor.in/SIDBI_Publications/Narsimham%20Committee.pdf

http://en.wikipedia.org/wiki/Herfindahl_index

http://law.jrank.org/pages/8543/Mergers-Acquisitions-Types-Mergers.html

Ibid

http://www.wisegeek.com/what-is-a-conglomerate-merger.htm

www.investorwords.com/80/acquisition.html
www.investorwords.com/4868/takeover.html

http://law.jrank.org/pages/8543/Mergers-Acquisitions-Types-Mergers.html

http://www.learnmergers.com

http://en.wikipedia.org/wiki/List_of_bank_mergers_in_the_United_States