

Special reference to merge Nedungandi bank Ltd on base of a case study about merging banks

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Abstract: A banking merger is just the same as the merger of two companies except that it involves banks. Mergers and Acquisitions (M&A) in the banking sector may be in the form of amalgamation, absorption, consolidation, acquisition or take over. The important point in the bank merger is that banking activities of the participants will always be regulated. In the present study efforts have been made to analyse the effects of M&A on the Financials of the Merger of Nedungadi Bank Ltd. (NBL) With Punjab National Bank (PNB) before and after merger. For this purpose various variables namely, capital, deposits, investments, advances, interest earned, interest paid, total income, total expenditure and net profit have been identified. In the analysis of variables figures for four year prior to merger and figures of variables for four years after the merger have been taken. Figures prior to merger are the total of value of variables of both amalgamating bank (the bank which loses its identity) and amalgamated bank (the bank which continues its existence). The result of regression equation has been found effective after merger of PNB and NBL from the point of view of capital, deposits, advances, interest earned and total income. In the case of investments, fixed assets, interest expenditure, total expenditure, net profit and total assets result of regression equation has been found ineffective. The Null Hypothesis is rejected in all variables except capital, fixed assets and interest expenditure.

Keywords: Merger, Acquisition, Capital, Deposits, Investments, Advances, Fixed Assets, Interest Earned, Interest Paid, Total Income, Total Expenditure, Net Profit and Total Assets

1. Introduction

Mergers and Acquisitions (M & A) has become such an integral part of corporate business strategy that now every company is a possible target for an acquisition or a merger. A banking merger is just the same as the merger of two companies except that it involves banks. M & A in the banking sector may be in the form of amalgamation, absorption, consolidation, acquisition or takeover. The important point in the bank merger is that banking activities of the participants will always be regulated. The rationale and the driving factors behind the consolidation process might have undergone change inter-temporally and varied across countries, two distinct dimensions broadly emerge from the history of bank consolidations, viz., market driven *vis-à-vis* government led consolidation. The challenges facing the India banking industry could be classified under three Cs Competition, Convergence and Consolidation.

These Cs will be the key drivers of the banking sector in the days ahead.

2. Objective of the Study

The study has been under taken to examine to evaluate the effectiveness of merger of the Nedungadi Bank Ltd. (NBL) With Punjab National Bank (PNB) on the basis of selected variables.

2.1. Period of Study

In order to make a comparison of the performance of the NBL with PNB, data for four years prior to merger and data for four years after the merger have been analyzed. Thus, a period of nine years has been analyzed.

2.2. Methods of Analysis/Research Methodology

The analysis has been made on the basis of the Mean,

Standard Deviation, Growth Rate and 't' Test of different variables before and after merger. In order to ensure the significance of change in mean value before and after merger t-test has been used at 5% level of significance and 8 Degree of freedom. The predicted values of identified variables have been calculated by using regression equation ($y = a + bx$) and presented in tables and charts.

2.3. Hypothesis

The present work is essentially based on secondary sources; hence hypothesis is being tested by using published materials. For the purpose of study *Null Hypothesis* is that there is no difference in mean value of selected variables before merger and after merger and *Alternate Hypothesis* is that there is difference in mean value of selected variables before merger and after merger.

Let Mean value before merger be X1

Mean value after merger be X2

Ho: $X1 = X2$ Null Hypothesis: There is no difference in mean value of selected variables before merger and after merger.

H1: $X1 \neq X2$ Alternate Hypothesis: There is difference in mean value of selected Variables before merger and after merger.

3. Variables

In order to judge the effectiveness of mergers and acquisitions of Merger of Nedungadi Bank Ltd. (NBL) With Punjab National Bank (PNB) following 11 variables have been identified:

- ❖ Capital: Capital represents the resources contributed by owners. The capital includes share capital and undistributed profits. The growth of capital indicates capacity of banks to attract deposits, lend to the business unit and to borrow from the public. One of the aims of merger is to increase the capital base of the banks. It is expected that the banks after merger would have sufficient capital base.
- ❖ Deposits: The important element of conventional banking business is to accept deposits from the customers. One of the important sources of lending money is deposit. Without deposits the bank cannot provide the loan in different sectors. For the purpose the study the deposits refer to the bank balances in different accounts.
- ❖ Investments: Investment refers to the investment of funds in the different areas such as government securities, subsidiary companies, mutual funds and others which are shown in the assets side of balance sheet of banks. The main purpose of such investment is either to earn a return or/ and to control another company. The investment helps to increase the total revenue and profit of the banking industry.
- ❖ Advances: Advances is the another important aspect

of conventional banking operations. In this study total advances include term advances, short term advances, advances to assisted company, advances to priority sector, advances in public sector etc

- ❖ Fixed Assets: Fixed assets represent the economic resources that are used to generate future earnings. Fixed assets refer to the net fixed assets. Without fixed assets it is impossible to run the banking industry. It is assumed that there would be positive impact on the fixed assets after the merger.
 - ❖ Interest Earned: One of the main sources of income of banking industry is the interest earned.
 - ❖ Total Income: The revenue earned from the different sources is total income. In the case of banking industry interest income is the main income. However, for the purpose of this study, total income refers to interest received, dividend received, security transactions, exchange transaction, commission and brokerage etc. it is expected that the total income will be increased after the merger and acquisition.
 - ❖ Interest expenditure: Interest provided to customer in different saving and fixed deposits accounts and interest of debt capital is the interest expenditure. The interest expenditure can be minimized by increasing the operating efficiency. The operating efficiency can be increased by merger and acquisition.
 - ❖ Total Expenditure: The expense incurred to operate the bank is the total expenditure. The total expenditure should be controlled to increase the profitability. By increasing the operating efficiency the total expenditure can be reduced. It is possible by M&A.
 - ❖ Net Profit: The profit is an indicator of the efficiency with which the business operations are carried out by corporate sector. The poor operational performance may result in poor sales leading to poor profits. The merger intends to boost profits through elimination of overlapping activities and to ensure savings through economies of scale. The amount of profit may be increased through reduction in overheads, optimum utilization of facilities, raising funds at lower cost and expansion of business.
 - ❖ Total Assets: Assets represent economic resources that are the valuable possessions owned by a firm. Assets are mainly used to generate earnings. The total assets refer to net fixed assets and current assets. One aim of business strategy namely, merger and acquisition is, the maximization of total assets of merged banks i.e., firms' ability to produce large volume of sales revenue. It is expected that the bank units after merger would function efficiently.
- PUNJAB NATIONAL BANK (PNB), the first Indian bank started only with Indian capital, was registered on May 19, 1894 under the Indian Companies Act with its

office in Anarkali Bazaar Lahore. PNB was nationalized in July 1969 and currently the bank has become a front-line banking institution in India. The corporate office of the bank is at New Delhi. The Bank is the second largest Government-owned commercial bank in India next to SBI and 3rd largest bank in the country (after SBI and ICICI Bank) and has the 2nd largest network of branches (4668 including 238 extension counters and 3 overseas offices). One of the major achievements of the Bank is covering all the branches (100%) of the Bank under Core Banking Solution (CBS), with more than 2150 ATMs. It serves over 38 million customers. The bank has been ranked 239th biggest bank in the world by The Bankers (June 2009), London. Apart from offering banking products, the bank has also entered the credit card & debit card business; bullion business; life and non-life insurance business; gold coins & asset management business, etc.

NEDUNGADI BANK LTD. (NBL) established as a commercial bank at Calicut in Kerala in 1913 by late Rao Bahadur T.M. Appu Nedungadi, author of Kundalatha, one of the earliest novels in Malayalam. The Bank being the first commercial bank to be set up in South India, took over selected assets and liabilities of the Coimbatore National Bank Ltd., in 1965. With branches at all major metropolitan cities like New Delhi, Calcutta, Chennai, Mumbai, Ahmedabad etc., Nedungadi Bank has almost widened its operations to a truly national level.

Capital Inadequacy and a high level of Non-Performing Assets (NPA) were the main factors that led the century-old private sector Nedungadi Bank Limited into a severe financial crisis forcing the centre to put the bank under moratorium. Nedungadi Bank, which has 175 branches and 1,619 employees, reported a net loss of Rs.678 million in the year ended March 31, 2001. NBL has taken over by PNB in 2003. At the time of the merger with PNB, Nedungadi Bank's shares had zero value, with the result that its shareholders received no payment for their shares. It was a forced merger under the direction of Reserve Bank of India (RBI) and Government of India (GOI).

4. Main Reasons/ Motives of Merger

- Capital Inadequacy and a high level of NPA was main reason of merger.
- Productivity per employee of NBL was low.
- RBI merged sick bank with healthy bank to protect depositor's interests.
- RBIs move to weed out the Broker promoter Rajendra Bhatia from bank, hold 32 per cent stake in Nedungadi Bank.

Financials of the Nedungadi Bank Ltd. and Punjab National Bank at the time of Merger (2002-03)

S.No.	Financial Indicators of Banks	Nedungadi Bank Ltd. (Rs. in crore)	Punjab National Bank (Rs. in crore)
1.	Capital	0010.20	00376.73
2.	Deposits	1438.06	64123.48
3.	Investments	0527.94	28207.17
4.	Advances	0769.88	34369.42
5.	Total assets	1577.09	72914.67
6.	Net Profit	0001.27	00562.39

Source: Compiled from Balance Sheet of Respective Banks.

(i) Capital

Table 1. Actual and Predicted Values of Capital of NBL & PNB (During 1999 to 2007)

Year	Capital (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	222	240
2000	222	253
2001	222	266
2002	222	278
2003@	265	291
2004	265	304
2005	315	316
2006	315	329
2007	315	341

Source: Extracted and computed from the annual reports of RBI and IBA
Y*: Regression equation ($y = a + bx$)
@:- Year of Merger

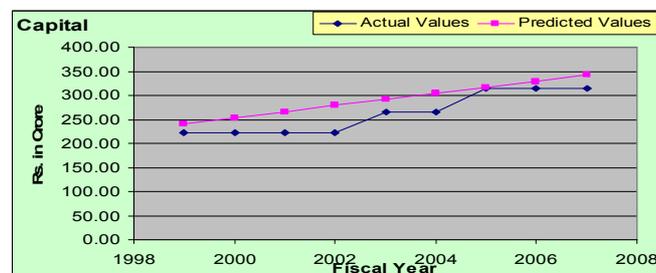


Figure 1. Capital and its Predicted Values

Table 1 shows the actual value of capital and its predicted values of Punjab PNB and NBL over a period of study. The Table reveals that the difference of capital and its trend value is negative throughout study period. However, the negative deviation during the post merger period is lower than the pre merger period which indicates that the effective performance of the Punjab National Bank after merger in comparison to before merger.

Figure 1 shows the actual and predicted value of capital. The curve of actual capital shows a fluctuating trend. It is constant till 2002 and thereafter it increases. The curve of actual capital is lower than the curve of trend value throughout study period.

(ii) Deposits

Table 2 portrays the actual value of deposits and its predicted value of PNB and NBL during the period of study.

Table 2. Actual and Predicted Values of Deposits of NBL & PNB (During 1999 to 2007)

Year	Deposits (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	041960	043909
2000	049071	054308
2001	057880	064707
2002	065561	075106
2003@	075813	085505
2004	087916	095904
2005	103167	106303
2006	119685	116702
2007	139860	127101

The Table shows that the difference of deposits and its trend value is negative in the year 1999 to 2005 while these are positive in the year 2006 and 2007. The positive difference in 2007 is very large while the negative difference is very large in 2003. The actual value of deposits is lower than predicted value throughout study period except 2006 and 2007. With regard to deposits, it has found that there is improvement during post merger period. Figure 2 shows the actual and predicted value of deposits. The curve of actual values shows an increasing trend of deposits. The curve of actual deposits is higher than the curve of trend value in 2006 and 2007.

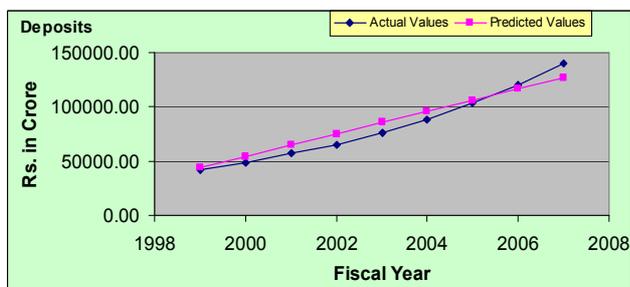


Figure 2. Deposits and its Predicted Values

(iii) Investments

Table 3 demonstrates the actual value of investments and its predicted value of PNB and NBL during the period under review. The table clearly depicts that the difference of investments and its trend value is negative in the year 1999 to 2003 and 2006, 2007 while these are positive in the year 2004 and 2005. The positive difference in 2005 is very large while the negative difference is very large in 2006. The actual value of investments is lower than predicted value before merger whereas it is higher than predicted value after merger except in 2006 and 2007. The performance of the Punjab National Bank is unsatisfactory

during post merger period in comparison to pre merger period with regard to investments.

Figure 3 shows the actual and predicted value of investments. The curve of actual value shows a fluctuating trend of investments. It increases continuously till 2004. Further, it decreases sharply in 2006. The curve of actual investments is higher than the curve of trend value in 2004 and 2005 only.

Table 3. Actual and Predicted Values of Investments of NBL & PNB (During 1999 to 2007)

Year	Investments (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	19050	21795
2000	22648	25707
2001	25833	29619
2002	28735	33530
2003@	34030	37442
2004	42125	41353
2005	50673	45265
2006	41055	49177
2007	45189	53088

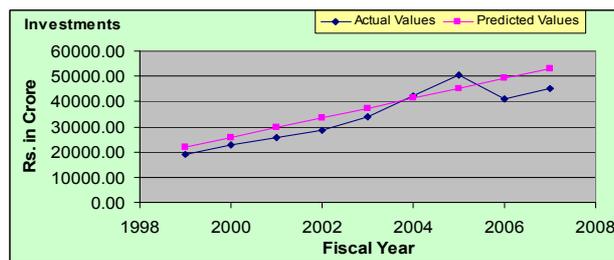


Figure 3. Investments and its Predicted Values

(iv) Advances

Table 4 presents the actual value of advances and its predicted value of PNB and NBL over a period of study.

Table 4. Actual and Predicted Values of Advances of NBL & PNB (During 1999 to 2007)

Year	Advances (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	19692	17800
2000	23365	25095
2001	28877	32391
2002	35139	39686
2003@	40228	46981
2004	47224	54277
2005	60413	61572
2006	74627	68867
2007	96596	76163

The Table reveals that the difference of advances and its trend value is negative in the year 2000 to 2005 while these

are positive in the year 1999, 2006 and 2007. The positive difference in 2007 is very large while the negative difference is very large in 2004. With regard to the advances, the performance of the Punjab National Bank has improved during the post merger period. Figure 4 shows the actual and predicted value of advances. The curve of actual value shows an increasing trend of investments. The curve of actual advances is higher than the curve of trend value in 1999, 2006 and 2007.

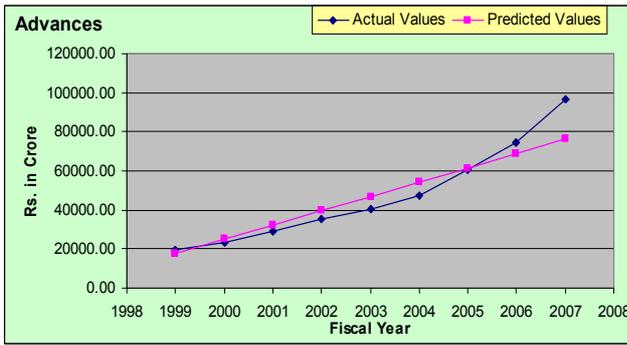


Figure 4. Advances and its Predicted Values

(v) Fixed Assets

Table 5 contains the actual value of fixed assets and its predicted value of PNB and NBL during the study period. The Table clearly shows that the difference of fixed assets and its trend values are negative throughout the study period. The result shows that the performance of the Punjab National Bank with regard to the fixed asset has unsatisfactory during after merger period.

Table 5. Actual and Predicted Values of Fixed Assets of NBL & PNB (During 1999 to 2007)

Year	Fixed Assets (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	630	747
2000	703	796
2001	754	846
2002	789	895
2003@	884	945
2004	899	994
2005	965	1044
2006	1030	1093
2007	1009	1143

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation (y = a + bx) @-: Year of Merger

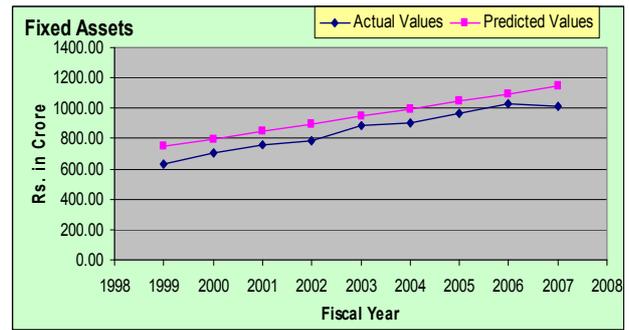


Figure 5. Fixed Assets and its Predicted Values

Figure 5 shows the actual and predicted value of fixed assets. The curve of actual value shows an increasing trend of fixed assets. It increases continuously till 2006. The curve of actual fixed assets is lower than the curve of trend value throughout the study period.

(vi) Interest Earned

Table 6 illustrates the actual value of interest income and its predicted value of PNB and NBL over a study period. The Table reveals that the difference of interest income and its trend value are negative throughout the study period except in 2007. The result shows that the performance of the Punjab National Bank with regard to the interest income has improved after merger. Figure 6 shows the actual and predicted value of fixed assets. The curve of actual value shows an increasing trend of interest income. The curve of actual interest income is higher than the curve of trend value in 2007 only.

Table 6. Actual and Predicted Values of Interest Income of NBL & PNB (During 1999 to 2007)

Year	Interest Income (Rs. in Crore)	Y* (Predicted Values) Rs. in Crore
1999	04594	05417
2000	05327	06035
2001	06040	06653
2002	06803	07271
2003@	07485	07889
2004	07779	08507
2005	08460	09126
2006	09584	09744
2007	11537	10362

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation (y = a + bx) @-: Year of Merger

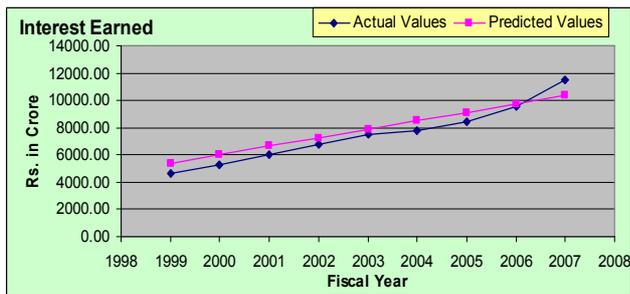


Figure 6. Interest Income and its Predicted Values

(vii) Total Income

Table 7 delineates the actual value of total income and its predicted value of PNB and NBL during the period under the study. The Table shows that the difference of total income and its trend values are negative throughout the study period except in 2007. However, the negative deviation during pre merger period is higher than the post merger period which indicates improvement in performance of the Punjab National Bank after merger.

Table 7. Actual and Predicted Values of Total Income of NBL & PNB (During 1999 to 2007)

Year	Total Income (Rs. in Crore)	Y* Predicted Values (Rs. in Crore)
1999	05156	06123
2000	06080	06886
2001	06848	07649
2002	07850	08412
2003@	08735	09175
2004	09646	09938
2005	10136	10701
2006	10857	11464
2007	12579	12227

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation ($y = a + bx$) @:- Year of Merger

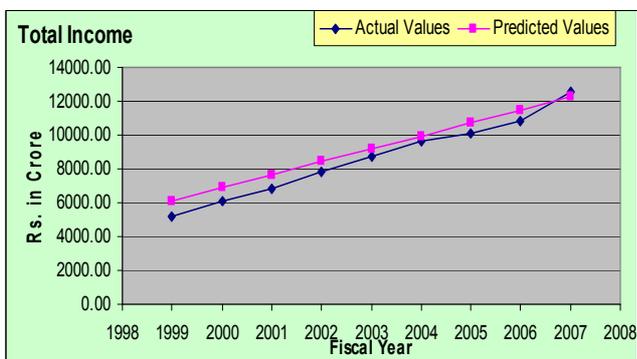


Figure 7. Total Income and its Predicted Values

Figure 7 shows the actual and predicted value of total income. The curve of actual value shows a fluctuating trend of total income. The curve of actual total income is higher than the curve of trend value in 2007 only.

(viii) Interest Expenditure

Table 8. Actual and Predicted Values of Interest expenditure of NBL & PNB (During 1999 to 2007)

Year	Interest Paid (Rs. in Crore)	Y* Predicted Values (Rs. in Crore)
1999	2908	3875
2000	3663	4057
2001	3982	4238
2002	4497	4420
2003@	4361	4601
2004	4154	4782
2005	4453	4964
2006	4917	5145
2007	6022	5327

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation ($y = a + bx$) @:- Year of Merger

Table 8 exhibits the actual value of interest expenditure and its predicted value of PNB and NBL during the study period. The difference of interest expenditure and its trend value is negative throughout the study period except in 2002 and 2007. Good performance of the Punjab National Bank has observed during post merger period except 2007.

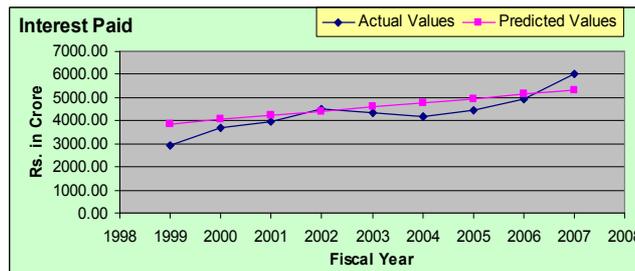


Figure 8. Interest Paid and its Predicted Values

Figure 8 shows the actual and predicted value of interest expenditure. The curve of actual values shows a fluctuating trend of interest expenditure. The curve of actual interest expenditure is higher than the curve of trend value in 2002 and 2007 only.

(ix) Total Expenditure

Table 9. Actual and Predicted Values of Total Expenditures of NBL & PNB (During 1999 to 2007)

Year	Total Expenditure (Rs. in Crore)	Y* Predicted Values (Rs. in Crore)
1999	04322	05444
2000	05233	05860
2001	06178	06276
2002	07063	06693
2003@	07893	07109
2004	08538	07525
2005	08725	07942
2006	09418	08358
2007	11426	08774

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation ($y = a + bx$) @:- Year of Merger

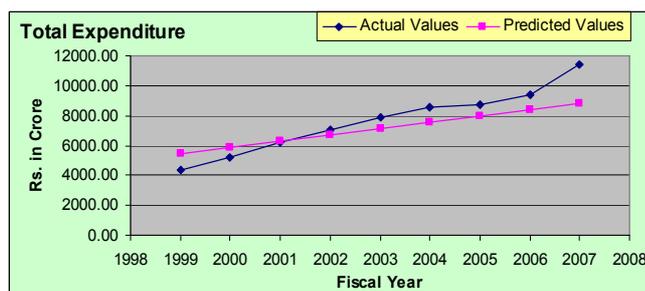


Figure 9. Total Expenditure and its Predicted Values

Table 9 displays the actual value of total expenditure and predicted value of PNB and NBL over a study period. It is clear from the Table that the difference of total expenditure and its trend value is negative in 1999 to 2001 while positive in 2002 to 2007. The negative difference is very large in 1999. The result shows that the bad performance of the Punjab National Bank during post merger period. Figure 9 shows the actual and predicted value of total expenditure. The curve of actual values shows an increasing trend of total expenditure. The curve of actual total expenditure is higher than the curve of trend value in 1999, 2000 and 2001 only.

(x) Net Profit

Table 10. Actual and Predicted Values of Net Profit of NBL & PNB (During 1999 to 2007)

Year	Net Profit (Rs. in Crore)	Y* Predicted Values (Rs. in Crore)
1999	0380	0274
2000	0422	0443
2001	0395	0613
2002	0563	0783
2003@	0842	0953
2004	1108	1123
2005	1410	1293
2006	1439	1462
2007	1540	1632

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation ($y = a + bx$) @:- Year of Merger

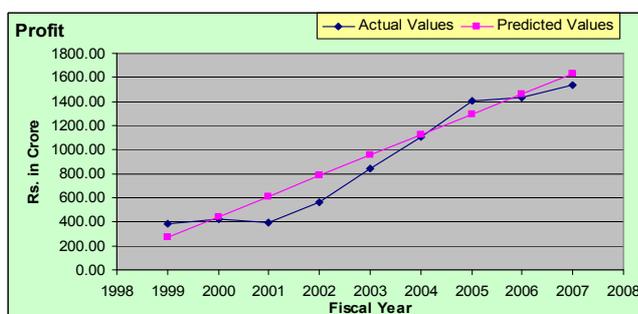


Figure 10. Net Profit and its Predicted Values

Table 10 discloses the actual value of net profit and its

predicted value of PNB and NBL during the period under the review. The table shows that the difference of profit and its trend value is negative in the year 2000, 2001, 2002, 2003, 2004, 2006 and 2007 while these are positive in the year 1999 and 2005. The positive difference in 2005 is very large while the negative difference is very large in 2001. The profitability of the Punjab National Bank has not been improved during the post merger period.

Figure 10 shows the actual and predicted value of net profit. The curve of actual profit shows fluctuating trend. The curve of actual profit is higher than the curve of trend value in 1999 and 2005 only.

(xi) Total Assets

Table 11 depicts the actual value of total assets and its predicted value of PNB and NBL during study period.

Table 11. Actual and Predicted Values of Total Assets of NBL & PNB (During 1999 to 2007)

Year	Total assets (Rs. in Crore)	Y* Predicted Values (Rs. in Crore)
1999	047631	047486
2000	055867	060712
2001	065405	073939
2002	074491	087166
2003@	086221	100392
2004	102332	113619
2005	126241	126846
2006	145267	140073
2007	162422	153299

Source: Extracted and computed from the annual reports of RBI and IBA
 Y*: Regression equation ($y = a + bx$) @:- Year of Merger

The difference of total assets and its trend value is negative in the year 2000, 2001, 2002, 2003, 2004 and 2005 while these are positive in remaining year 1999, 2006 and 2007. The positive difference in 2007 is very large while the negative difference is very large in 2003. The result shows that the performance of the Punjab National Bank has improved after merger. Figure 11 shows the actual and predicted value of total assets. The curve of actual value shows an upward trend of total assets. The curve of actual total assets is higher than the curve of trend value in 1999, 2006 and 2007.

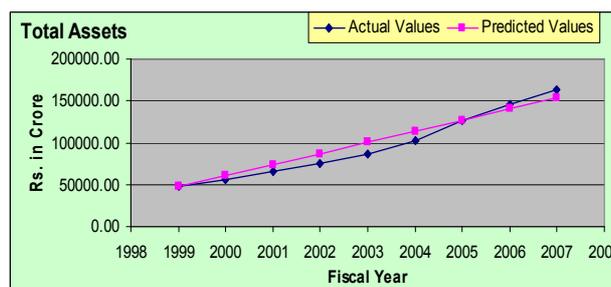


Figure 11. Total Assets and its Predicted Values

Hypothesis Analysis

In this section, the mean, standard deviation, growth rate and 't' values of different variables have been calculated and presented, before merger and after merger, to examine the impact of M&A on different variables. For the processing of the data, Excel and SPSS-10 package in computer have been used. In order to ensure the significance of change in mean values before and after merger 't' test has been used.

Changes in Average Value Different Variables and its Variability in Merged Bank

S. No	Different Variables	Mean		t Value	Growth Rate
		Before	After		
1	Capital	222.44 (82.25)	295.3 (98.87)	0.61*	33%
2	Deposits	53618.37 (10285.87)	105288.31 (19004.54)	3.98	96%
3	Investment	24067.01 (4166.93)	42614.67 (6822.67)	4.48	77%
4	Advances	26768.64 (6737.30)	63817.87 (15183.65)	3.47	138%
5	Fixed Assets	719.49 (69.30)	957.97 (74.49)	1.65*	33%
6	Interest Earned	5691.54 (947.47)	8908.97 (932.06)	3.97	57%
7	Total Income	6483.89 (1144.06)	10391.07 (874.79)	4.65	60%
8	Interest Expenditure	3763.16 (665.24)	4781.66 (322.04)	1.92*	27%
9	Total Expenditure	5450.16 (879.33)	8303.81 (793.45)	2.88	52%
10	Net Profit	440.61 (571.91)	1267.97 (281.41)	3.23	188%
11	Total Assets	60849.13 (11639.23)	124496.70 (26020.00)	3.80	105%

@Figures in bracket are Standard Deviation. *insignificant

Table shows the mean value of capital, deposits, investments, advances, fixed assets, interest earned, interest paid, total income, total expenditure, net profit and total assets before and after merger and its variability, growth rate of average value of 11 variables before and after merger and 't' values. The result presented in table clearly shows that all 11 variables have shown a significant growth during post-merger period than the average value during pre-merger period. It shows that merger of NBL with PNB

have earned significant growth in Net profits (188%) and Advances (138%) than other 9 variables. The Null Hypothesis is rejected in all variables except capital, fixed assets and interest expenditure.

Summary of Results/Conclusion

The result of regression equation has been found effective after merger of PNB and NBL from the point of view of capital, deposits, advances, interest earned and total income. In the case of investments, fixed assets, interest expenditure, total expenditure, net profit and total assets result of regression equation has been found ineffective. The Null Hypothesis is rejected in all variables except capital, fixed assets and interest expenditure.

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Biography



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