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Impact of Merger in Share Price Announcement and Financial Performance – Banking Sector

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ABSTRACT

Merger and Acquisition are important strategic tool in the banking sector, it helps the Indian bank as well as the Indian economy by maintaining the bank healthy. This study helps to identify the impact of the merger in stock price announcement and also examine the growth rate impact of pre- and post-merger period. The event study methodology is used to identify the impact of merger in stock price announcements in Mega merger banks. The financial ratio is used find the growth rate impact of pre- and post-merger period. The findings of the study are merger gave negative impact to the Canara, Indian bank, positive impact to the Punjab national bank and Union Bank of India.

Keywords: *Merger & Acquisition, Stock price, financial performance, Banking sector, financial ratio, Event window analysis*

INTRODUCTION

A merger occurs when two or more entities join forces to establish a new, combined organization. An acquisition refers to the purchase of one firm by another. (Hasen and Solama, 2015). Mergers and acquisitions (M&As) are two of the most frequent business tactics for expanding a company, allowing sectors and organizations to benefit from economies of scale and increase their market competitiveness.

History of Merger in India

S.no	Bank	Merged with	Year of merger
1	Mahila bank	SBI	2017
2	State bank of Bikaner and Jaipur	SBI	2017
3	State bank of Patiala	SBI	2017
4	State bank of Hyderabad	SBI	2017
5	State bank of Travancore	SBI	2017
6	State bank of Mysore	SBI	2017
7	Dena bank	Bank of Baroda	2019
8	Vijaya bank	Bank of Baroda	2019
9	Syndicate bank	Canara bank	2020
10	Allahabad bank	Indian bank	2020
11	United bank of India	PNB	2020
12	Oriental bank of commerce	PNB	2020
13	Andhra bank	Union bank of India	2020
14	Corporation bank	Union Bank of India	2020

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Mega Merger is Needed?

According to the Ministry of finance, Need of a Mega-Merger such as

- Manage capital more efficiently
- Restructure & Redefine country's banking space
- Creation of global-sized banks

Challenges and contribution

Due to increase in globalisation, attainment of size advantages will become critical for Indian banks. It is further combined with the need to attain higher capital standards under Basel II Accord, consolidation in the Indian Banking industry will become imminent. Hence the following issues need to be addressed. It includes maximizing synergies in terms of regional balance, network of branches, HR culture, and asset commonality and legacy issues in respect of technology. In the present scenario, we must develop small number of large banks of global size instead of large number of smaller banks as we are having at present.

Statement of the Problem

Merger and acquisition activities in India looks promising one that is driven by many factors like conutry's growing economy, increasing foreign investment and favourable regulatory environment. Hence the present study focuses on analyzing the impact of mega mergers and its financial performance in banking sector. The Event Window analysis was used to assess the impact of mega mergers in Indian banking sector.

Objective of the study

To analyze the impact of pre- and post-merger and acquisition announcements of Canara bank, Indian bank, Punjab national bank, Union bank of India in stock price.

Review of Literature

[1] study the disparities in stock price reaction to merger announcements between target and acquiring corporations. "The cumulative returns have exhibited a downward trend in the post-merger era, reflecting a negative effect of the combination," they found. [4] investigated the impact of takeovers on acquirers' intrinsic value and concluded that M&As damage investors on the acquiring side. [5] looked at the cash flow performance of the 50 largest US companies after they merged. The study found that post-merger cash flow growth did not come at the price of the merging businesses' long-term sustainability, since the sample firms kept their capital spending and R&D rates in line with their industry. [8] used financial metrics to examine the post-merger financial performance of combined institutions. In the post-merger and acquisition process, strategies and policies in procedural, physical, and socio-cultural contexts were shown to be highly essential variables. [7] investigated the post-merger effect on bank performance in India, concluding that bank mergers are effective and advantageous to the newly merged business, as well as shareholders and customers. [9] looked at how M&A announcements affected stock prices. They come to the conclusion that CAAR has a beneficial influence on the post-merger period and that the event has a major impact on the stock price. [2] investigated mergers and acquisitions and their success variables, concluding that M&A success is linked to M&A partners' relative size, managerial involvement, culture, and organizational culture concerns.

Research Methodology

The study used a descriptive research approach with a purposive sampling. A total of 10 public sector banks would be included in the study. For ten public sector banks, secondary data was used to collect 365-day stock price data.

1. Descriptive Statistics (Mean)

It is used to analyze the pre- and post-merger impact in Abnormal Returns.

2. Financial Ratio

To identify the pre- and post-Merger Growth impact by using net profit ratio

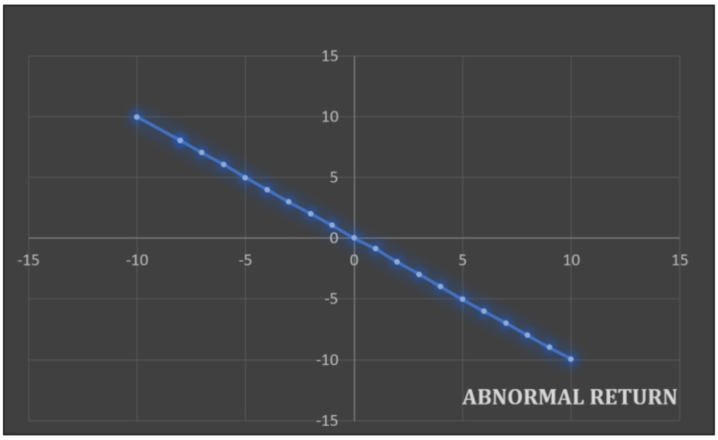
$$\textbf{Net profit margin (\%)} = \frac{\textbf{Profit after tax}}{\textbf{Sales or revenue}}$$

3. Event Study methodology

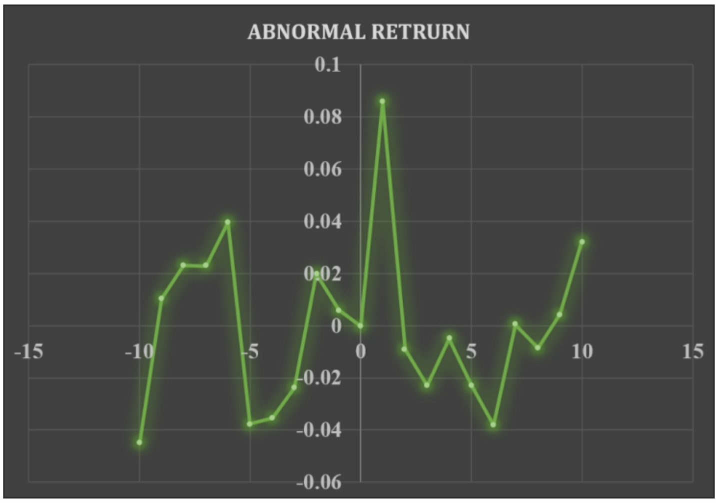
It is used to track the changes in stock prices of publicly traded corporations in response to certain events or announcements. It was created by Fama in 1969. The anomalous returns approach is widely used to quantify the change in stock prices of publicly traded firms in response to particular events or event notifications. The purpose of the event analysis is to determine the additional profits or losses that stockholders will experience as a result of their participation in the event. The anomalous return is a measure for post-acquisition shareholder value growth.

Abnormal return = Actual return – Expected return
Expected return = $\alpha + \beta^*$ Market return
Actual return = Actual return is closing stock price value of respective bank

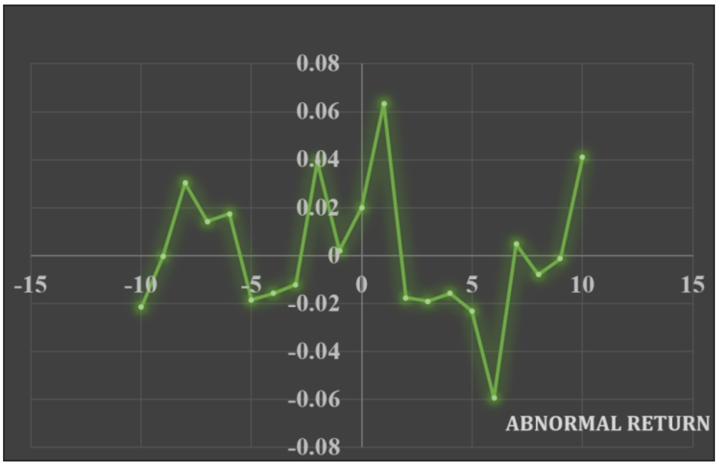
RESULTS AND DISCUSSION



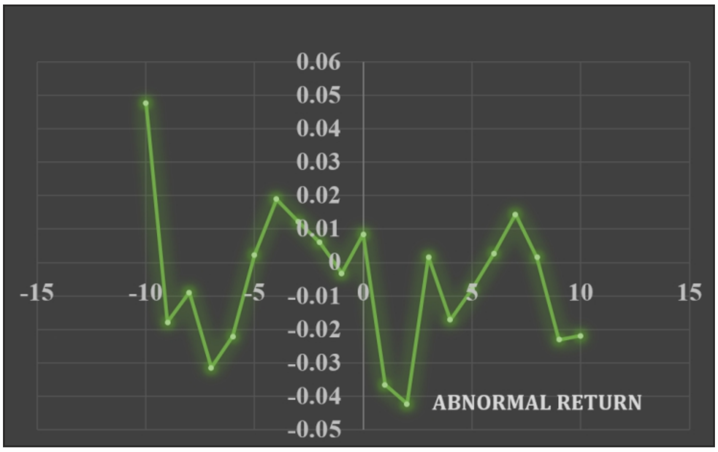
Canara Bank stock price attains sharp decline on both Pre and Post merge, but in pre merge period stock price flow in positive only, after announcement stock price goes to negative (Event impact: Negative).



Punjab national bank stock price flow both positive and negative in pre and post merge period, but the maximum price attains after the announcement date only (Event impact: Positive).



Union bank of India stock price flows both positive and negative in pre and post merge period, but maximum price attains after announcement date only (Event impact: Positive).



Indian bank stock price flows in both positive and negative in pre and post-merger period, but the maximum price is attained before the event period. (Event impact: Negative).

Conclusion

Bank	Abnormal Rate of Return	Mega Merger Impact	Mega Merger Impact
	Pre-Merger (Mean)	Post- Merger (Mean)	
Canara Bank	5.396	-5.486	201 percent (Decrease)
Punjab National Bank	-0.00203	0.001587	178 percent (Increase)
Union Bank of India	0.003471	0.00353	3 percent (Increase)
Indian Bank	0.000355	-0.01289	102 percent (Decrease)

Reason for the negative impact of canara bank and Indian bank, Acquired bank (Syndicate bank Bank & Allahabad bank) NPA is more than 5 % and its financial strength is instable so it make a burden to the acquiring bank (Indian bank and Canara bank) so merger announcement gives the negative impact to the respective banks.

Reason The reason for the positive impact of union bank of India and Punjab national bank, Merger is completely different because normally two banks are only involved in the merger, but for UBI & PNB is merge with two public sector banks (1{strongest bank} + 2 {weakest bank} = Strongest single entity). This type of merger creates more positive impact. The merger creates a high capital bank, global competitive strength, more infrastructure etc.

Future Scope

The Indian financial system requires very huge investment banks to absorb several risks that have appeared from operating in local international bank. The prime aspects for future mergers in Indian banking industry includes the challenges of free convertibility and requirement of large banks for investments. Therefore the Government and policy makers should be more thoughtful in endorsing mergers which paves way to gain economies of scale and scope.

Annexure

Event window analysis for Canara Bank

EVENT WINDOW	ABNORMAL RETURN
10	-9.95591
9	-9.00072
8	-8.00214
7	-6.99821
6	-6.03504
5	-5.0342
4	-4.00277
3	-2.99685
2	-1.97922
1	-0.88934
0	-0.00233
-1	1.025496
-2	2.009094
-3	2.972197
-4	3.965619
-5	4.965
-6	6.044487

-7	7.022811
-8	8.023237
-8	8.019133
-10	9.949328

Event window analysis for Punjab National bank

EVENT WINDOW	ABNORMAL RETRURN
10	0.032157
9	0.004314
8	-0.00857
7	0.000404
6	-0.03815
5	-0.02301
4	-0.00499
3	-0.02288
2	-0.00912
1	0.085716
0	-0.00019
-1	0.005948
-2	0.019681
-3	-0.02379
-4	-0.03531
-5	-0.03757
-6	0.039519
-7	0.022874
-8	0.022932
-9	0.010406
-10	-0.045

Event window analysis for Union bank of India

EVENT WINDOW	ABNORMAL RETURN
10	0.040965
9	-0.00127
8	-0.00795
7	0.00476
6	-0.05948
5	-0.02309
4	-0.01579
3	-0.01916
2	-0.01759
1	0.063346
0	0.019921
-1	0.002107
-2	0.039234
-3	-0.01208
-4	-0.01583
-5	-0.01858
-6	0.017405
-7	0.014208
-8	0.030218
-9	-0.00043
-10	-0.02154

Event window analysis for Indian bank

EVENT WINDOW	ABNORMAL RETURN
10	-0.02197
9	-0.02312
8	0.001516
7	0.014337
6	0.002647
5	-0.00793
4	-0.01713
3	0.001678
2	-0.04228
1	-0.03662
0	0.008421
-1	-0.00321
-2	0.006024
-3	0.012216
-4	0.019007
-5	0.002336
-6	-0.02213
-7	-0.03149
-8	-0.00901
-9	-0.01787
-10	0.047674

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