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Post-Merger Financial Performance Analysis of ICICI Bank and Erstwhile Bank of Rajasthan Ltd.

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The corporate sector, be it Services or Manufacturing globally is restructuring its operations through mergers and acquisitions in an unprecedented manner. This phenomenon is more predominant in hypercompetitive markets like India. Indian companies like HDFC Bank, ICICI bank, Airtel etc are reckoned as global competitors in their sectors. These Indian firms have also learnt that inorganic growth is a faster mechanism. M&As are used by corporate sector to eye the units all around the operational region which, in-turn, will help them restructure financially. The driving force is restructuring the corporate entities financially through the medium of M&As.

Since Mergers and Acquisitions have emerged as a natural process of business restructuring throughout the world and financial restructuring through mergers and acquisitions evokes a great deal of public interest and perhaps represent the most dynamic facet of corporate strategy and evolution, the researcher found it suitable to study the impact of mergers and acquisitions on financial performance vis Value Creation of Indian companies. For the purpose the researchers have taken the case of merger/acquisition from the Banking sector -- ICICI Bank - Bank of Rajasthan Ltd.

Key Words: Merger and Acquisition, BFSI, Banking Sector, Financial Performance

Introduction

Concept of Merger & Acquisition:

- **A merger** is the combination of two or more companies into one, wherein merging entities lose their identities. No fresh investment is made through this process. However, an exchange of shares takes place between the entities involved in such process. Generally, the company that survives is the buyer which retains its identity and the seller company is extinguished.
- **An acquisition,** alternately, is aimed at gaining a controlling interest in the share capital of the acquired company. It can be enforced through an agreement with the persons holding majority interest in the company's management or through purchasing shares in the open market or purchasing new shares by private treaty or by making a take-over offer to the general body of shareholders.

Differentiating features of Merger & Acquisition:

- In practice actual mergers of equals don't happen very often. Usually, one company will buy another and, as part of the deal's terms, simply allow the acquired firm to proclaim that the action is a merger of equals, even if it is technically an acquisition. Being bought out often carries negative connotations, therefore, by describing the deal euphemistically as a merger, deal makers and top managers try to make the takeover more palatable.
- Whether a purchase is considered a merger or an acquisition really depends on whether the purchase is friendly or hostile and how it is announced.
- A takeover, which is essentially an acquisition, differs from a merger in its approach to business combinations. In the process of takeover, the acquiring company decides the maximum price that is to be offered to the acquired and hence takes lesser time in completing a transaction than in mergers, provided the top management of the acquired company is co-operative.
- In merger transactions, the consideration is paid for in shares whereas in a takeover, the consideration is in the form of cash.

Mergers and Acquisition in India during post liberalization era:

A recent KPMG study found that only 30% of cases of M&A in India created shareholders value. In 39% of such deals, there was no discernible difference, while in 31% of cases the shareholder's value was diluted. The finding though shocking to most, stems from imperfections, which exist in most economies and more distinctly in India.

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The Indian banking sector, which far too many loss making units, could have possibly benefit from mergers but M&As have failed to perform. The efficient operation of the takeover mechanism requires that vast quantities of information to be widely available, which is not the case in India. Besides, there is a huge transaction costs involved in takeovers, which hamper the efficiency of the mechanism. If a firm's operation is or is perceived to be a symmetric, it may pay rational managers even in rational markets to be narrow minded. This would lead to short term measures and to lower rates of investment than would otherwise be the case. The first to be hit in the circumstance is the shareholder's value.

Review of Literature

Rao, Narsimha,V, and Rao, P,V, Krishna(1987) attempts to evaluate the impact of such mergers on the performance of a corporation. Though the theoretical assumption says that mergers improve the overall performance of the company due to increased market power, the author uses his paper to evaluate the same in the scenario of Indian economy. He has tested three parameters – PBITDA, PAT and ROCE - for any change in their before and after values by comparison of means using t-test.

Agrawal, A., Jaffe, J.F., Mandelker, G.N. (1992) in their paper, have tried to evaluate the efficiency and performance for selected public and private banks before and after the merger, as a results of market forces. After doing a factor analysis, they narrow down the variables for their study to Profit Margin, Current Ratio, Ratio of Advances to Total Assets, Cost Efficiency (ratio of cost to total assets)and Interest Cover and thereafter a regression is run to identify the relationship between these factors and return on shareholders funds.

Anand & Singh (2008) study the effect of five specific mergers in the Indian banking sector on the shareholders wealth. These are mergers of the Times Bank with the HDFC Bank, the Bank of Madurawith the ICICI Bank, the ICICI Ltd. with the ICICI Bank, the Global Trust Bank with the Oriental Bank of Commerce, and the Bank of Punjab with the Centurion Bank..

Fisher, Alan A. and Robert H. Lande, (1983) test the hypothesis that horizontal mergers generate positive abnormal returns to stockholders of the bidder and target firms because they increase the probability of successful collusion among rival producers. Under this hypothesis, rivals of the merging firms benefit from the merger since successful collusion limits the output and raises product prices and/or lower factor prices

Andrade, G., Mitchell, M., Stafford, E. (2001) have studied the impact of mergers on the operating performance of acquiring corporates in different industries, by examining some premerger and post-merger financial ratios, with the sample of firms chosen as all mergers involving public limited and traded companies in India between 1991 and 2003. Their results suggest that there are minor variations in terms of impact on operating performance following mergers, in different industries in India. In particular, mergers seem to have had a slightly positive impact on profitability of firms in the banking and finance industry, the pharmaceuticals, textiles and electrical equipment sectors saw a marginal negative impact on operating performance. In more than 5,763 mergers and acquisitions between 2002 and 2011, acquiring institutions purchased more than $6 trillion in assets globally.

Goyal and Joshi (2011) probed the motives of banks for mergers and acquisition with special reference to Indian Banking Industry and the study was conducted on the basis of number of branches, geographical penetration in the market and benefits from the merger.

Goyal and Joshi (2012a) studied the growth of ICICI Bank Ltd. through mergers, acquisitions, and amalgamation. Mergers and acquisitions (M&As) are considered as corporate events which helps an organization to create synergy and provide sustainable competitive advantage, but, simultaneous these sorts of corporate events have the potential to create severe personal trauma and stress which can result in psychological, behavioural, health, performance, and survival problems for both the individuals and companies, whether it is a bank or a non banking financial corporation, involved in it. It is evident from the case of ICICI Bank Ltd. that how an organization can become market leader by adopting some strategic tools like mergers and acquisitions.

----- (2012b) attempted to identify the general sentiments, challenges and opportunities for the Indian Banking Industry. According to the authors the biggest challenge for banking industry is to serve the mass market of India. Companies have shifted their focus from product to customer. The banks understand their customers, the more successful they will be in meeting customers' needs. In order to mitigate above mentioned challenges Indian banks must cut their cost of their services. Another aspect to encounter the challenges is product differentiation.

- **Research Methodology**

Objectives of the Study:

The study has been undertaken to contribute towards the following broad Objectives:

1. To make a comparative analysis of the impact of mergers on financial performance of the selected entity of BFSI industry in India.

Importance of the study:

Mergers and Acquisitions (M&As) have been for years, the principal tools of corporate restructuring and one is to witness a sharp increase in both the number and size of the M&A transactions in the country. Financial restructuring through mergers and acquisitions evokes a great deal of public interest and perhaps represent the most dynamic facet of corporate strategy. Taking into consideration these important facts, the researcher have undertaken this study.

Hypothesis of the Study:

The following hypotheses have been formulated and tested to draw the conclusions:

- H0: There is no considerable difference between pre and post merger financial performance.
- H1: There is a considerable difference between pre and post merger financial performance.

Sample Size and Sample Selection:

The researcher has selected a convenient sample of 01 company merged in the BFSI sector.

Acquirer Company	Targeted Company	Year	Deal Value
ICICI Bank	Bank of Rajasthan	2009-10	667 Mn USD

Highlight:

The sample company from Indian banking sector was merged with 100% stake.

Period of Study:

The researchers have made an attempt to study the impact of Mergers on financial performance of the sample company by using the available information for the period

2006-07 to 2010-11.

Data Collection:

After defining the objectives & hypothesis we need to look at the type and sources of data and other specific information needed to attain the said objectives. The present study is mainly based on secondary data which have been collected through annual reports of the companies, books & journals, news papers & magazines and websites etc. The data of just preceding years of the year the merger took place has been considered for pre-merger study and the data for the year 2010-2011 has been used for post merger study.

Tools and Techniques:

To analyze the available financial information to study the company, various techniques of applied research and accounting tools like comparative ratios have been employed. The following 6 major financial ratios and their means were calculated for analyzing the financial performance of the sample case:

- Operating Profit Ratio (OPR)

  Net Profit Ratio (NPR)
- Earnings Per Share(EPS)

  Debt -Equity Ratio
- Return on Investment (ROI)

  Dividend Payout Ratio (DPR)

These average ratios were compared using Paired Sample 't' test. A confidence interval of 95% has been set for difference in means.

Introduction of The Sample Merger Case:

Icici Bank Acquired The Bank of Rajasthan

(Year of Merger: 2009-10)

ICICI Bank

- Private sector lender Bank of Rajasthan on 18 may 2010 agreed to merge with ICICI Bank, India's second largest private sector lender ,Bank of Rajasthan had a market value of $296 million. The acquisition of Bank of Rajasthan by ICICI bank was the first consolidation of country's crowded banking sector since 2008. ICICI Bank and Bank of Rajasthan (BoR) boards cleared their merger through an all-share deal, valued at about 30.41 billion rupees.
- ICICI offered BoR 188.42 rupees per share, in an all-share deal, for Bank of Rajasthan, a premium of 89 percent to the small lender's closing price on the previous day, valuing the business at $668 million. ICICI offered the smaller bank's controlling shareholders 25 shares in ICICI for 118 shares of Bank of Rajasthan.
- The Big Deal :The deal, which would give ICICI a sizeable presence in the northwestern desert state of Rajasthan, valued the small bank at about 2.9 times its book value, compared with an Indian banking sector average of 1.84.Bank of Rajasthan had a network of 463 branches and a loan book of 77.81 billion rupees ($1.7 billion).

PRE-POST MERGER FINANCIAL PERFORMANCE OF SAMPLE MERGER CASE

ICICI BANK AND BANK OF RAJASTHAN LTD. (YEAR OF MERGER: 2009-10)

Table showing the financial results of ICICI Bank and Bank of Rajasthan Ltd. during pre and post merger period

Ratios	Pre- Merger Period								Post- Merger Period	
	Acquirer or Parent company (ICICI Bank)				*Acquired or Target Company* (Bank of Rajasthan Ltd.)					
	2006-07	2007-08	2008-09	Avg.	2006-07	2007-08	2008-09	Avg.	2010-11	Avg.
Operating Profit Ratio (%)	28.87	26.00	26.22	27.03	28.84	21.18	21.12	23.71	24.81	24.81
Net Profit Ratio (%)	10.81	10.51	9.74	10.35	12.56	9.75	7.81	10.04	15.91	15.91
Return on Investment (%)	82.46	62.34	56.72	67.17	140.81	173.00	185.2	166.44	42.97	42.97
Earnings per Share	34.59	37.37	33.76	35.24	10.28	8.57	7.30	8.72	44.73	44.73
Dividend Payout Ratio (%)	28.91	29.43	32.58	30.31	19.45	5.83	2.74	9.34	31.29	31.29
Debt-Equity Ratio	9.50	5.27	4.42	6.39	25.37	26.15	23.60	25.04	4.10	4.10

Source: Published Financial Statements of the Company

Analysis of The Financial Results:

- The above table shows the position of ICICI Bank and Bank of Rajasthan Ltd during pre and post merger period. ICICI Bank acquired Bank of Rajasthan Ltd, raising the share Value of ICICI Bank to new heights and making the former a stronger bank with a stronger balance sheet.
- When we start comparing the ratios of both the banks pre and post merger, one very important ratio which indirectly tells the strength of the companies operation is operating ratio which was 27.03% for ICICI bank pre merger while it was 23.71% for Bank of Rajasthan. Post merger the ratio changed to 24.81% indicating a decline. This clearly indicates that the Company has realized some losses which might be due to the high costs incurred during the merger period.
- Talking about the Net ratio for the acquirer Company before merger was 10.35% while the net profit ratio for the acquired company was 10.04%. During post merger the average Net profit ratio was 15.91% which shows a significant increase from 10.35% to 15.91% and a clear communication that the company has made profits after merger. It can be suggested that the company has gained monopoly and the advantages of goodwill are helping the company gain some substantial profit.
- The pre-merger average for ROI for the acquirer Company was 67.17% while the return on investment for the acquired company was 166.44%. Post merger the average return on investment declined to 42.97. Also the average of Net worth before merger for the acquiring Company was 9.89% while the return on net worth for the target company was 22.96%. After merger the average on return on net worth slightly declined to 9.35% for the acquired company. This indicates that less was incurred at the time of merger.
- Taking the financial condition of the bank in consideration average earnings per share during pre-merger for ICICI Bank was (35.24) while that of the target company was

(8.72). Post merger the average earnings per share increased to (44.73). This might be attributed that the shareholders had retained some profits or dividends to make the company a stronger financial organization.

- The operating ratio, return on investment has indicated a slight decline in their performance. The company has shown potential in attaining high profits as the main parameter i.e. net profit ratio, earning per share have shown significant increase in their performance.
- Further the table shows that dividends payout ratio average was 30.31% for the acquirer Company while of the target company it was 9.34%. After Merger the payout ratio changed to 31.29%. This indicates a very slight increase in the post merger period for the acquirer company from 30.31% to 31.29%. The average of debt-Equity ratio before merger for the acquirer company was 6.39 and that of the target company was 25.04. Post merger the ratio had declined to 4.10.

Financial Indicator Wise-Analysis

➢ Operating Profit Ratio of ICICI Bank

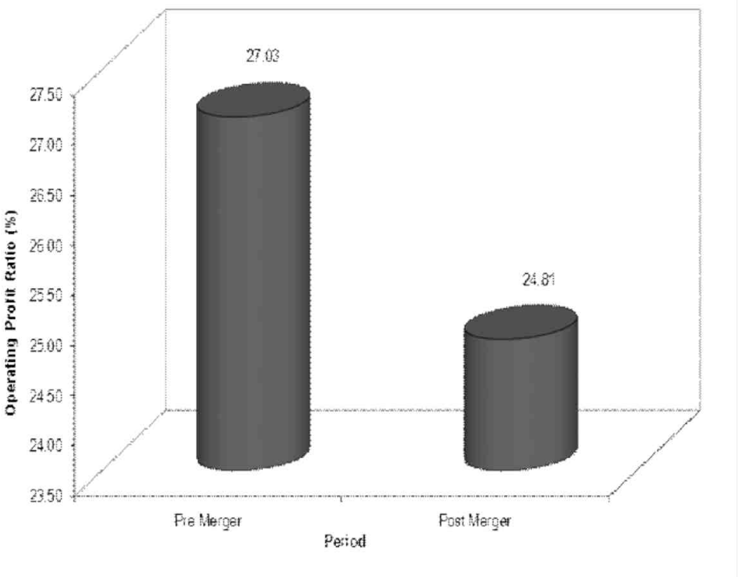
Period	N	Mean	SD	t	df	Result
Pre Merger	3	27.030	1.597	1.204	2	NS
Post Merger	1	24.810	0.000			

The operating profit ratio for ICICI bank before merger was 27.030. After merging The Bank of Rajasthan Ltd in to it this ratio was decreased to 24.810. The test for difference of mean was found to be non significant (t = 1.204 < tab = 2.920 at 5% level of significance).

Hence the hypothesis taken '**There is a considerable difference between pre & post merger financial performance**' is accepted.

The above position has graphically been presented as below:-

Pre & Post merger Operating Profit Ratio position of ICICI Bank



➢ Net Profit Ratio of ICICI Bank

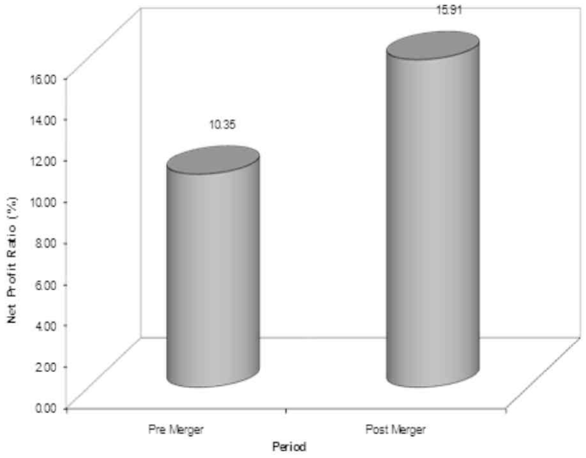
Period	N	Mean	SD	t	df	Result
Pre Merger	3	10.353	0.552	-8.719	2	*
Post Merger	1	15.910	0.000			

The Net Profit Ratio for ICICI Bank Ltd. was 10.353 in the pre merger period which was slightly increased to 15.910 in the post merger period. The difference in the net profit ratio between pre merger and post merger period was found to be significant (t = 8.719 > ttab = 2.920 at 5% level of significance).

Hence the hypothesis taken '**There is a considerable difference between pre & post merger financial performance**' is proved to be rejected.

The above position has graphically been presented as below:-

Pre & Post merger Net Profit Ratio position of ICICI Bank



- **Return on Investment of ICICI Bank**

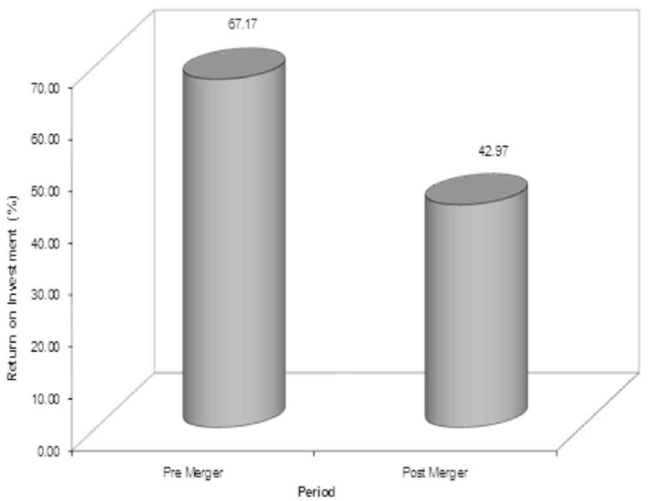
Period	N	Mean	SD	t	df	Result
Pre Merger	3	67.173	13.534	1.549	2	NS
Post Merger	1	42.970	0.000			

Return on Investment for ICICI Bank Ltd. was 67.173 in the pre merger period. In the post merger period after merging The Bank of Rajasthan Ltd. in to it this operating profit ratio of ICICI Bank Ltd. was came down to 42.970 (t = 1.549 < ttab = 2.920 at 5% level of significance).

A sharp decline in mean ROI after merger proves that the hypothesis taken '**Mergers in Indian Corporate sector in general resulted in value addition to shareholders**' is accepted.

The above position has graphically been presented as below:-

Pre & Post merger ROI Ratio position of ICICI Bank



- **Earning Per Share of ICICI Bank**

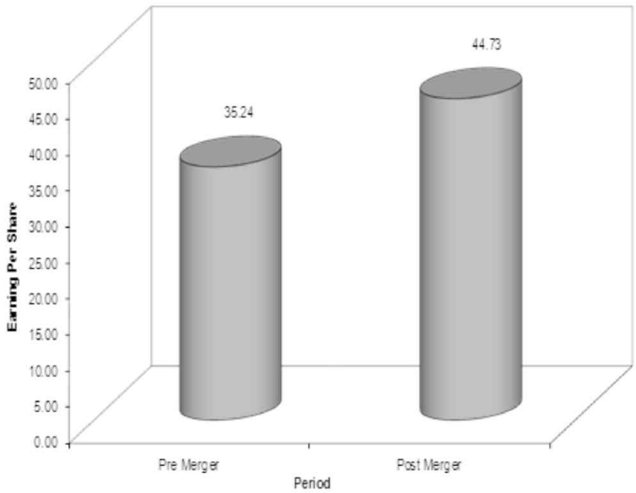
Period	N	Mean	SD	t	df	Result
Pre Merger	3	35.240	1.891	-4.347	2	*
Post Merger	1	44.730	0.000			

Earnings per share for ICICI Bank Ltd were 35.240 in the pre merger period. After merger this figure was increased to 44.730. The test for difference of means was applied between pre merger and post merger situation. The test results show that the difference is significant (t = 4.347 > ttab = 2.920 at 5% level of significance).

Hence the hypothesis taken '**Mergers in Indian Corporate sector in general resulted in value addition to shareholders**' is rejected.

The above position has graphically been presented as below:-

Pre & Post merger EPS Ratio position of ICICI Bank



- **Dividend Payout Ratio of ICICI Bank**

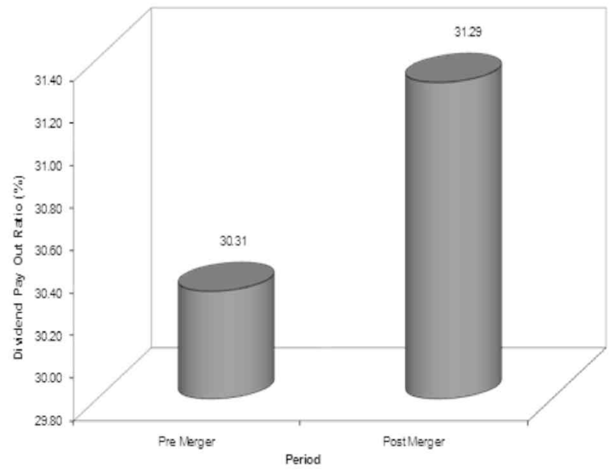
Period	N	Mean	SD	t	df	Result
Pre Merger	3	30.307	1.986	- 0.429	2	NS
Post Merger	1	31.290	0.000			

Dividend payout ratio for ICICI Bank Ltd in the pre merger situation was 30.307 which are slightly increased to 31.290 in the post merger period. The test for difference of means was found to be non significant (t = 0.429 < ttab = 2.920 at 5% level of significance).

Hence the hypothesis taken '**Mergers in Indian Corporate sector in general resulted in value addition to shareholders**' is accepted.

The above position has graphically been presented as below:-

Pre & Post merger Dividend Payout Ratio position of ICICI Bank



- **Debt Equity Ratio of ICICI Bank**

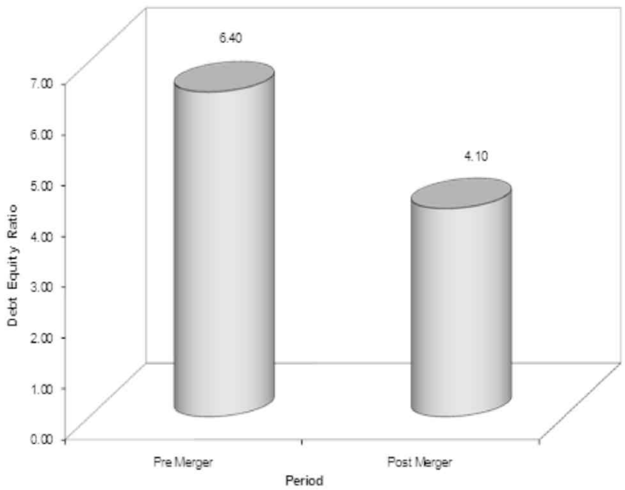
Period	N	Mean	SD	t	df	Result
Pre Merger	3	6.397	2.721	0.731	2	NS
Post Merger	1	4.100	0.000			

The mean debt equity ratio for ICICI Bank Ltd before merger was 6.397. After merger this ratio was came to figure of 4.100. The difference in the pre merger and post merger period was found to be non significant (t = 0.731 < ttab = 2.920 at 5% level of significance).

Hence the hypothesis taken '**There is a considerable difference between pre & post merger financial performance**' is accepted.

The above position has graphically been presented as below:-

Pre & Post merger Debt Equity Ratio position of ICICI Bank



Limitations of The Study:

Though researchers have made a humble attempt to encompass the pre and post merger performance of the selected sample merger case, it is difficult to narrate all incidents and changes brought up due to mergers and acquisitions and therefore necessary inferences are inserted wherever required.

Secondly, the study is based purely on secondary data which are taken from the financial statements of the case through Internet only and therefore can't be denied for any ambiguity in data used for the analysis.

Conclusions:

On the basis of analytical study of sample merger case, the following conclusions have been drawn which are perfectly in the line of objectives predetermined:

- From the shareholders point of view of Profitability the sample company attained positive results in the post merger period.
- The earnings growth after merger was found at the much higher rate resulted in value addition to shareholders.
- A substantial dividend growth was observed after merger in Sample Company.

Suggestions:

After concluding the results of this study, it is found appropriate to put the following suggestions:

1. It is observed on the basis sample study that the small and medium sized banking entities are working under threats from economic environment which is full of problems like inadequacy of resources, outdated technology, non-systematized management pattern, faltering marketing efforts and weak financial structure etc. It is therefore advised to re-organize such industries through merger/acquisitions so that they could offer succor to re-establish them in viable industries of optimal size with global presence.
2. It is also suggested that corporate mergers / acquisitions should be bound to change drastically and rapidly the economy in size and quality performance through re-organized undertakings, combined resources and united efforts of experienced executives and skilled workforce.

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