1. Merger of Public Sector Banks

Prelims: Economics- Banking

Mains: GS-III- Indian Economy and Issues Relating to Planning, Mobilization of Resources, Growth, Development and Employment.

- **Context:** The Centre has announced a mega amalgamation plan, aimed at improving their financial health and enhancing their lending capacity to support growth.

Highlights:

- The merger announcement was followed by an equity infusion move of Rs 55,250 crore in these banks to enable them to grow their loan book. With these series of mergers, the number of state-owned banks is down to 12 from 27.
- There are four new sets of mergers — Punjab National Bank, Oriental Bank of Commerce and United Bank of India to merge to form the country's second-largest lender; Canara Bank and Syndicate Bank to amalgamate; Union Bank of India to acquire Andhra Bank and Corporation Bank; and Indian Bank to merge with Allahabad Bank.

The Logic Behind the Mergers:

- According to the government, banks have been merged on the basis of likely operating efficiencies, better usage of equity and their technological platform.
- But the move marks a departure from the plan to privatise some of the banks or bringing in a strategic investor to usher in reform in the sector.
- The government, after consultations, decided that amalgamation is the "best route" to achieve banking sector scale and to support the target of achieving a $5 trillion economic size for India in five years.
- Analysts note that the amalgamations will help banks to meaningfully scale up operations but will not lead to any immediate improvement in their credit metrics.

Previous Experience with the Mergers:

- Last year, the government had merged Dena Bank and Vijaya Bank with Bank of Baroda, creating the third-largest bank by loans in the country.
- The government said this merger has been "a good learning experience" as **profitability and business of the merged entity has improved**.

- Earlier, the State Bank of India had acquired its associate banks. Indian Overseas Bank, UCO Bank, Bank of Maharashtra and Punjab and Sind Bank, which have strong regional focus, will continue as separate entities.
- In a presentation on the proposals, the government said **profitability of public sector banks has improved and total gross non-performing assets have come down**.

Will the Merger Help Improving the Performance?

- According to the analysts, while the announced consolidation of PSU banks is credit positive as it enables the consolidated entities to meaningfully improve scale of operations and help their competitive position, at the same time, there will not be any immediate improvement in their credit metrics as all of them have relatively weak solvency profiles.
- In the present case, the mergers are mostly among larger banks, with absorbing bank not necessarily in strong health.
- However, given the merged banks are on similar technology platform, the integration should be smoother.
- Also, it is likely that management attention and bandwidth of the entities being merged could get split impacting the loan growth and reduce focus on strengthening asset quality in the short term.