Bank amalgamation: Is it much ado about nothing?

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The govt's proposal to amalgamate Dena, Bank of Baroda and Vijaya Bank has immediate gains, but key issues remain

HYDERABAD, SEPTEMBER 18

The government's move to amalgamate Bank of Baroda, Dena Bank and Vijaya Bank may have immediate gains but leaves key systemic challenges unresolved.

In a way, the smooth absorption of five associate banks and Bharatiya Mahila Bank with State Bank of India (SBI), which was completed last year, must have encouraged the government to go ahead with another round of consolidation of public sector banks.

The merger of banks is not an economic taboo. The Committee on Banking Sector Reforms (the Second Narasimham Committee - 1998) had also suggested mergers among strong banks, both in the public and private sectors, and even with financial institutions and NBFCs.

As per Reserve Bank of India data, since the beginning of the economic reforms in 1990, there have been 22 bank amalgamations (excluding SBI associate banks' merger last year), triggered by different circumstances.

Interestingly, weak banks were merged before 1999, but later, there have been mergers between healthy banks, driven by business and commercial considerations.

Today's scenario is similar to that before 1999 as the banks proposed to be amalgamated have weak fundamentals. Hence, the proposal has both merits and demerits.

Main advantages

Rationalisation of branches, re-deployment of manpower and cost-reduction are seen as main advantages. Surely, one can expect closure of some branches once the amalgamation materialises.

Generally, as part of the consolidation process, the combined entity would be more inclined to shift its branches and focus of operations from rural to urban and semi-urban areas, which are usually more remunerative.

This will have to be avoided in this new round of consolidation.

Operations

The claim of the government that the amalgamation will drive higher lending to corporates and improve customer service has to be taken with a pinch of salt.

Lending is a dynamic function of banking based on sound principles of repayment, but not entirely decided by the size of the balance sheet.

The sluggishness in corporate lending has been not as much because of the smaller size of banks as due to wilful default, stressed assets and the macro economic environment.

As the net non-performing assets (NPA) ratio of the amalgamated entity will he higher (than the present NPA ratio of BoB and Vijaya Bank individually) at 5.71 per cent, it remains to be seen how this will lead to a better lending scenario, going forward.

So, without addressing the systemic challenge of bad loans, mere amalgamation of those banks which had higher bad loans may not deliver the desired growth in banking operations.

It remains to be seen if consolidation of public sector banks will finally pull the banking sector out of the woods. Edit P8

Published on September 18, 2018

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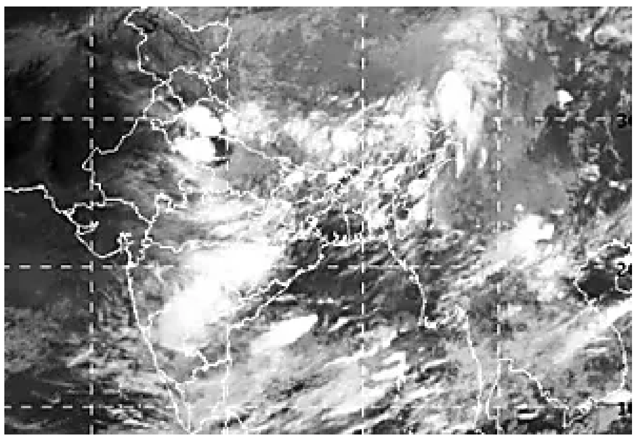

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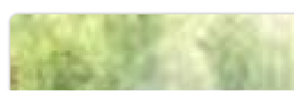

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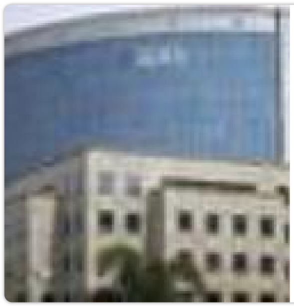

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