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Market Watch

# India plans mega banks but analysts say bet on rivals instead

BY BLOOMBERG | UPDATED: SEP 03, 2019, 10.55 AM IST

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By **Abhishek Vishnoi and Ameya Karve**

Equity analysts predict that India's move to merge several of its state banks will slow their loan growth, and many brokers advise buying shares of the lenders' rivals who stand to benefit from the uncertainty.

While the mergers will reduce the number of state-owned banks to 12 from 27 and are aimed at creating bigger and healthier lenders, the time needed for integration and challenges related to staff, branch and process overlaps are expected to be the main immediate risks.

Prime Minister Narendra Modi's government late Friday surprised analysts by announcing a series of mergers that will create four new lenders that will hold business worth 55.8 trillion rupees (\$781 billion), or about 56% of the Indian banking industry. The announcement came minutes before data showed economic growth in Asia's third-biggest economy slumped to a six-year low of 5%, below the weakest estimate of 39 economists polled by Bloomberg.

Futures contracts on India's Nifty 50 Index dropped 1% in Singapore on Monday, when local markets were shut, indicating the broader stock market may decline when they open for trade on Tuesday.

Here is what some of the analysts are saying:

## Caution on Merger Candidates

Mergers will keep state-run banks "busy in the integration process for a prolonged period and thus help private banks further consolidate their business market share," Emkay Global analysts Anand Dama and Rahul Malani wrote in a note dated Sept. 3. Emkay downgrades Indian Bank to hold from buy, and maintains sell on [Punjab National Bank](#), Canara Bank and Union Bank, citing merger overhang. The analysts retain buy on SBI and a positive bias toward private banks, with [ICICI Bank](#) and HDFC Bank as top picks among large stocks.

## Value Lies Outside

"Consolidation comes with its own set of challenges in HR, process integration, branch rationalization," analysts led by Kunal Shah at Edelweiss Securities Ltd. in Mumbai, wrote in an investor note on Friday. "Ideally, value lies in places outside the involved banks and within this space, we like State Bank of India as it is better positioned to grow," they wrote.

## Loan Growth Slows

"We have observed that historically, when state-owned banks merge, smaller banks' loan-book growth slows sharply, as the primary focus of management shifts to integration," Vishal Goyal and Ishank Kumar, analysts at UBS Securities India Pvt., said in a note on Saturday. ICICI Bank Ltd. and Axis Bank Ltd. remain UBS's most-preferred picks.

## Smaller Lenders Lose

The mergers may not be favorable for the smaller lenders based on the share-swap ratios decided in past state-owned bank combinations, analysts led by Adarsh Parasrampur at Nomura Financial Advisory & Securities (India) Pvt., wrote in a note on Saturday. "We continue to prefer private corporate banks such as ICICI and Axis Bank and we see value in State Bank, where merger-related uncertainty will not be there."

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### Deepen Credit Crunch

“Consolidation is a good long-term move, but could weigh on near-term growth and potentially worsen the credit crunch,” analysts led by Sumeet Kariwala at [Morgan Stanley](#) wrote in a note on Monday. The brokerage remains underweight on Punjab National Bank and Canara Bank.

### Credit Growth Pangs

Mergers are “unlikely to revive credit growth,” [Credit Suisse](#) Group AG’s analysts Ashish Gupta and Kush Shah wrote in a note on Monday. “Given the limited flexibility on restructuring and rationalization, meaningful cost synergies from PSU bank mergers are unlikely,” the note added.

### Strengthening the System

[Citigroup](#) Inc. said the mergers “are significant and should strengthen the banking system in the medium to long term.” Fewer banks will mean the government’s capital infusion will be concentrated and will aid in talent management, analysts including Manish Shukla wrote in a note, upgrading shares of Bank of Baroda Ltd. to buy from neutral.

### Faster Bad-Loan Resolution

“Near-term impacts could potentially be slower growth but faster NPL resolution, while medium-term impacts could include lower lending spreads in segments where SOE banks are market leaders,” Goldman Sachs Group Inc. analyst Rahul Jain wrote in a note.

Brokerages on PSU Bank merger: Near-term pain, long-term gain

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