ISSN Print: 2394-7500
ISSN Online: 2394-5869
Impact Factor: 8.4
IJAR 2022; 8(6): 324-327
www.allresearchjournal.com
Received: 22-02-2022
Accepted: 13-04-2022

Sofia Hamid
Maharshi Dayanand Saraswati University, Pushkar By-Pass Road, Ajmer, Rajasthan, India

Dr. KK Swami
Maharshi Dayanand Saraswati University, Pushkar By-Pass Road, Ajmer, Rajasthan, India

Corresponding Author:
Sofia Hamid
Maharshi Dayanand Saraswati University, Pushkar By-Pass Road, Ajmer, Rajasthan, India

Merger of HDFC limited and HDFC bank: It's significance

Sofia Hamid and Dr. KK Swami

Abstract
Although, Merger of banks is not a new occurrence, yet it has received considerable limelight in the banking sector. this paper attempts to analyse the proposed mega merger announced on 4 April 2022, of two giant companies HDFC limited with HDFC Bank, also discuss its benefits, effects on other banks and concludes that Merger of HDFC limited with HDFC Bank would prove to be a win-win situation for both the companies due to the economies of scale, diversified product offerings cost synergies and balance sheet flexibility. After merger, combined capabilities of both entities will result in more profitability and both entities will utilise each other's strength to their merits. India's largest conglomerate would be produced through this merger, which lead to sell products to more than 68 million customers. Impact on the share prices is positive for both entities. Apart from this, the mega merger will prompt other banks towards mergers and acquisitions to maintain their market share. Furthermore, the market share gap between SBI and HDFC Bank will be narrow down after merger.

Keywords: Merger, Acuisitions, HDFC Bank, HDFC Limited, Banks

Introduction
Scheme of merger of HDFC bank and HDFC limited
HDFC Bank and HDFC Limited on 4th April 2022, announced the merger of one of the largest entities of Indian financial sector. HDFC Bank is the largest private sector bank in India while HDFC Ltd is the largest housing finance company in India. As per the reports of The Indian Express, both these entities will merge together to form an entity with combined balance sheet of rs 17.87 lakh crore and net worth of rs 3.3 lakh crore which will enable larger underwriting at scale. Furthermore, the Merger will increase the ability to cross-sell products to a larger customer base.
According to the deal, HDFC Limited, India's largest housing finance company with Assets Under Management (AUM) worth Rs 5.26 trillion and a market cap of Rs 4.44 trillion will merge with HDFC Bank, India's largest private sector bank by assets with a market cap of Rs 8.35 trillion [1].

Reason behind the merger of HDFC limited and HDFC bank
Since 2014, there have been talks regarding the merger of HDFC Limited and HDFC Bank. Therefore, the agreement has been in the works for several years however it did not materialise during 2015 because the regulatory framework was bit complicated and strict.
On April 4 HDFC Board announced that HDFC Limited and HDFC Bank will come under an agreement through which the parent company will transfer some part of its loans to the bank every quarter. Thus for HDFC Bank this will be the sole exposure to home loans venture.
Consequently, the transaction would be beneficial for both the HDFC Limited and HDFC Bank due to the complimentary nature of businesses, cost synergies specifically due to the home loan business.
The similarity between the regulations of Non-banking financial company's (NBFCs) and banks played a major role in the merger decision. Due to Non-banking financial company's higher-margin products, large pools of priority-sector customers and loans, and potential cross-selling opportunities are some of the reasons it is on the target list for acquisitions.

Furthermore, owing to the 2018 IL&FS crisis, RBI has been compelling Non-banking financial companies to run like banks. As banks maintain some portion of reserves, similarly RBI has been pushing NBFCs to keep some reserves for unforeseen circumstances and it also secure a broad base of liabilities. It also became tough to run as a NBFC after a certain threshold limit of rs 5000 crore. Hence, regulations governing banks are required for those NBFCs and mergers are necessary in these situations.
Other reason is that, though HDFC Bank is a strong private sector lender, it is poor in terms of mortgage lending space. On the basis of December 2021 figures, home loans included in loan book of HDFC Bank's product wise lending is only about 6.2 percent and another 4.5 percent is loan against property.
Home loans are extremely adhesive assets for banks because as soon as you receive the customer then he/she will stay with the bank for 15-20 years. Despite this under home loan section, HDFC Bank were losing clients to other institutions such as ICICI Bank and Kotak Mahindra Bank, other housing finance companies such as LIC Housing Finance, L&T Housing and IIFL Housing etc. are the strong player in the home loans space. But HDFC Bank was incapable in getting customers in home loan section. After merger HDFC Bank will be able to provide home loans to over 68 million customers of HDFC Bank. Thus, mortgages are considered as an important factor in the decision of merger.
Also, the recently announced deal wherein, Citibank India's consumer business will be acquired by Axis Bank, could encourage banks to turn to Mergers and Acquisitions in future.

Benefits of merger of HDFC limited and HDFC bank

Presently as on date 5 April 2022 HDFC Bank's loan is at ₹12-lakh crore. Thus, it would be a challenging task to increase its loan book on its own as it involve managing growth, profitability, asset quality hence, merging with a known entity HDFC Limited is evidently a safe easier and cost-effective alternative.
As per the Hindu report, after merger, there will be diversification in the loan book of merged HDFC entity as most of the loan will be mortgages. Furthermore, the home loan portion in the loan book of HFDC Bank would jump to 33% from 11% now. Consequently, HDFC Bank will become as India's second leading bank after merger.
SBI is the top leading bank in India. After merger, there would be a difference between HDFC Bank and SBI of about ₹6–7-lakh crore. And the difference between HDFC Bank and ICICI Bank, which is the third largest bank, would be over ₹10-lakh crore. Thus, HDFC Bank's position would be strong and substantial [2].
According to the live mint report if we look at an asset base of combined HDFC entity will be $340 billion, which is almost half the value of the State Bank of India, but it is twice to its near competitor, ICICI Bank. Soon after merger there will be approximately a 300-basis point bounce in loan market share and about 100 bps in deposits from the standalone HDFC Bank [3].
Merger would be beneficial for both the entities of HDFC. Liquidity will also increase for HDFC Limited which will be beneficial in facing stiff competitions in the market. Also, the customer base will increase which will lead to more potential cross selling opportunities. Proportion of unsecured loans in the loan book of HDFC Bank will be reduced which assist in increasing the capital base.
Furthermore, it will also benefit to leverage their distribution across urban, semi urban and rural areas.

Table 1: Benefits of merger of HDFC limited and HDFC bank

Particulars	HDFC Limited	HDFC Bank
Total Assets (in rs/ lakh crore)	6.23	19.3
Revenue (rs/crore)	35,681	1,16,177
Advances (in rs/crore)	5	12.68
Market Capitalisation (in rs/ lakh crore)	5	7.25
Branches	445	6342
Customers (in lakh)	2.7	680

Market capitalisation of HDFC limited and HDFC bank: (as on April 4, 2022)
Source: company investor presentation, BSE.

Swap ratio of the transaction and time required to execute the merger

As per The Indian Express reports, HDFC limited shareholders will receive 42 shares of HDFC bank for their 25 shares as on record date. The swap ratio works as 1:1.68 [1].
According to reports of The Times of India report, The Merger of HDFC limited and HDFC Bank will be expected to be completed over the next 12 to 18 months after completion of regulatory approvals and customary closing formalities. Hence the deal is expected to be completed by the end of FY24. Till then, both entities will continue to operate as an independent entities, as they are today [4].

Ownership structure and merger effect on stakeholders

CEO of HDFC Bank, Sashidhar Jagdishan, will lead the merged entity. HDFC Bank came under the last year's list of the World's Best Banks.
The HDFC board has approved the merger with HDFC Bank hence Post the merger, the subsidiary or associates of HDFC Limited will be transferred to HDFC Bank. HDFC Limited's shareholding in HDFC Bank will be lost completely after merger and HDFC Bank will be fully owned by public shareholders [1].
Existing shareholders of HDFC Limited will own the shares of HDFC Bank thus they will receive 41 % shares in the HDFC bank [1].
Although, there would be a fall in the profits, return ratios of HDFC Bank, the merger will provide a wide access to the loan base to the shareholders of HDFC Bank, which will ultimately enhance the quality of asset. Even if there is some issue in some sections of the loan book for eg. Agriculture loans, Ministry of micro, small and medium enterprises etc. it will not effect the entire asset quality due to its diversified structure after merger.

Cost effectiveness or not

Merger of HDFC Limited and HDFC Bank will result in long term benefits. The step of merger would prove to be cost effective in the long run and thus there will be reduction in the cost of pricing, cost of running business, cost of operations etc. operational efficiency of HDFC entity will increase however it will take time to happen.
In fact post the merger, the cost of statutory reserves will rise in the near future and a slightly low-yielding housing finance book will be combined with a loan book, which will yield a net interest margin of four per cent [2].

Consequently, HDFC Bank's financial status may not depict a good picture in the starting years of operations post the merger but it will emerge as a good move in the long run.

According to Fitch ratings article, proposed merger deal would be advantageous to both HDFC entities. HDFC Bank will own about 500 new branches which will increase its operating efficiency. Cost to income ratio of HDFC Limited is 10% whereas HDFC bank's cost to income ratio is 36%. Therefore after merger operational effectiveness will improve [5].

The ongoing merger will have an effect on competitiveness of banks as well and the probability of mergers and acquisitions among banks will also rise. As banks will thrive to achieve the market share gap through mergers and acquisitions.

Effect on share price

The proposed merger will likely to build India's third largest company on the basis of market capitalisation, after Reliance Industries and TCS.

The announcement of the merger resulted in sudden increase in the share prices of the two entities which were escalated by over 7 per cent in the early trading hours [1].

Effect on borrowers and depositors

As per the economic times report, there will be no change in the customers of HDFC Bank because the proposed entity will be that of HDFC Bank. But the case is not same with customers of HDFC Limited.

Once the merger starts, interest rate might come under revision on home loans. Furthermore, HDFC Bank may require HDFC Limited customers to update their KYC details and may also require cleints, particularly those paying instalments using post-dated cheques, to provide a new NACH mandate. So that the auto-debit of home loan EMIs continue easily post the merger [6].

HDFC Chairman Deepak Parekh described the merger as "a coming together of equals" and added that "our customers will be the biggest beneficiary."

"The merger makes the combined entity strong enough to not only counter competition but make the mortgage offering even more competitive," he said

According to Forbes India report, Saurabh Mukherjea, founder of Marcellus Investment Managers says that there are significant economies of scale in operating large scale financial services, in the form of data/technology, distribution muscle and the cost of capital. "Now, four large empires are being built out: HDFC Bank empire, Axis Bank empire, ICICI Bank empire and the Bajaj Finserv-Finance empire. It will put huge stress on everybody else who does not have this scale," Mukherjea says. "The bugle has sounded out loud and clear, either get big or die trying." It will thus pave the way for more mergers and acquisitions for the other banks and NBFCs [8].

Sashi Jagdishan, CEO & MD, HDFC Bank said "The proposed transaction ticks all the right boxes in terms of completion of product offerings, product leadership in home loans as with other retail assets products, distribution strength across the country and a customer base that can be leveraged to cross-sell a complete suite of financial products," furthermore "It is value accretive for all the stakeholders of both the organisations, including shareholders, employees and customers," [9].

Impact on public sector banks

Public Sector Banks will have to make serious efforts in order to maintain their market share. After the announcement of proposed merger, market share of banking sector has come into sharp focus.

Since the start of millennium, private sector banks have been persistently chipping away at the market share of public sector banks. hence, the ongoing merger of HDFC limited with HDFC Bank, when it fructifies, will intensify this process.

On December-end 2021, state-owned SBI and HDFC Bank owns a total loan book of ₹26,64,602 crore and ₹12,68,863 crore, respectively. Therefore, the difference between the two banks was ₹13,95,739 crore. While, the merger of HDFC limited with HDFC Bank will create a loan book of ₹5,25,806 crore consequently the difference between SBI and its nearest competitor will be reduced to ₹8,77,933 crore.

After analysing the growth rate of both banks in total advances on December-end 2022 is 8.47 per cent for SBI and 16.5 per cent for HDFC Bank. it indicates that in 3-5 years, private sector banks will go ahead of SBI in market share [10].

Consequently, SBI needs to needs to increase its efficiencies to maintain its number one position and focus on to improve the market share and profitability.

Conclusion

The proposed merger will reduce the gap size between HDFC Bank and SBI. Similarly, it would increases the gap between HDFC Bank with its other competitors, both in the public and private sectors. It might even indulge HDFC Bank's competitors in the private banking sector to turn to mergers – either between themselves or own non-banking finance companies. Further merger will assist HDFC Bank to setup housing loan portfolio and increase its customer base. Proposed Merger will have an effect in the whole financial sector. If it is successful it will lead to more mergers and acquisitions in future. While the regulatory attitude should be lenient to make it successful.

To conclude the proposed mega merger of HDFC Limited with HDFC Bank positively affects the health of the banking sector which will ultimately be helpful to the Indian economy.

References

1. Explained: Why are HDFC Limited and HDFC Bank merging, and what will be its impact?. The Indian Express. Accessed 15 May 2022. Available at: https://indianexpress.com/article/explained/explained-hdfc-limited-hdfc-bank-merger-impact-stock-market-7851786/.
2. All about HDFC-HDFC Bank merger. The Hindu Business line. Assessed on 12 May 2022. Available at: https://www.thehindubusinessline.com/blexplainer/all-about-hdfc-hdfc-bank-merger/article65292288.ece
3. HDFC-HDFC Bank merger to shake up financial sector, says Fitch. Live mint. Assessed on 8 May 2022. Available at: https://www.livemint.com/industry/banking/hdfchdfc-bank-merger-to-shake-up-financial-sector-says-fitch-11649760705022.html
4. Merger of HDFC entities to increase M&A prominence among banks: Fitch. The Times of India. Assessed on

18 may 2022. Available at: https://timesofindia.indiatimes.com/business/india-business/merger-of-hdfc-entities-to-increase-ma-prominence-among-banks-fitch/articleshow/90799397.cm
5. India's HDFC Bank-NBFI Merger to Shake-Up Sector Dynamics. FitchRatings. Assessed on 17 May 2022. Available at: https://www.fitchratings.com/research/non-bank-financial-institutions/indias-hdfc-bank-nbfi-merger-to-shake-up-sector-dynamics-12-04-2022
6. HDFC-HDFC Bank merger: What does it mean for depositors and borrowers?. Economic Times. Assessed on 20 may 2022. Available at: https://economictimes.indiatimes.com/wealth/save/hdfc-hdfc-bank-merger-what-does-it-mean-for-depositors-and-borrowers/articleshow/90951388.cms
7. India's HDFC And HDFC Bank Will Merge To Create Financial Giant. Forbes. Assessed on 13 may 2022. Available at:https://www.forbes.com/sites/yessarrosendar/2022/04/04/indias-hdfc-and-hdfc-bank-will-merge-to-create-financial-giant/?sh=6aaf84be623a
8. The science behind HDFC-HDFC Bank's mega merger. Forbes India. Assessed on 21 may 2022. Available at: https://www.forbesindia.com/article/take-one-big-story-of-the-day/the-science-behind-hdfchdfc-banks-mega-merger/74997/1
9. Parent HDFC to merge with HDFC Bank. The Hindu. Assessed on 17 May 2022. Available at: https://www.thehindu.com/business/parent-hdfc-to-merge-with-hdfc-bank/article65289828.ece
10. HDFC-HDFC Bank merger: It's a wake up call for competition. The Hindu. Assessed on 13 May 2022. Available at: https://www.thehindubusinessline.com/money-and-banking/hdfc-hdfc-bank-merger-its-a-wake-up-call-for-competition/article65308633.ece
11. www.bseindia.com
12. www.hdfcbank.com
13. www.hdfc.com