Concerns with BoB, Dena Bank and Vijaya Bank Merger

What is the issue?

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- The Union government recently proposed the merger of Bank of Baroda, Dena Bank and Vijaya Bank.
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- However, the grounds for the merger, at the time of banks' weakening trend, have raised serious concerns.
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What are the concerns highlighted?

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- **Implication** - After the merger announcement, shares of Bank of Baroda and Vijaya Bank fell significantly.
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- On the other hand, Dena Bank gained sharply.
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- Notably, Dena Bank is the bank in the worst financial situation among the three entities.
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- It is currently under the Reserve Bank of India’s *prompt corrective action* framework.
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- Unlike the other two banks, its shareholders are set to gain from being part of a new bank with greater financial strength.
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- But the weaker banks would make an unhealthy impact on the operations of the stronger one.
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- Clearly, forced mergers such as the current one make little business sense for the stronger banks.
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- **Bad loans** - The merger is part of the government’s efforts to consolidate the banking industry to overcome the bad loan crisis.

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- Asking healthy banks to take over weak banks appears to be the strategy to handle the bad loans crisis.

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- But they are less likely to solve the bad loan crisis that has gripped the banking system as a whole.

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- **Shareholders** - A dominant shareholder in the form of the government is dictating critical moves.

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- This impacts the minority shareholders as they are left with no say in the matter.

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- A merger as significant as this one should have been first discussed and approved in the board rooms of the banks concerned.

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What could be a cautious move?

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- Undeniably, there are too many public sector banks in India and so consolidation is a good idea in principle.

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- But ideally, mergers ought to be between strong banks.

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- It is important to ensure that such mergers do not end up creating an entity that is weaker than the original pre-merger strong bank.

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- Certainly, mergers are just one way of managing the problem and therefore cannot be discounted totally.

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- However, the trick lies in ensuring that the merger fallout is managed prudently.

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- Identifying synergies and exploiting scale efficiencies will be crucial here.

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Source: The Hindu

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Quick Fact

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Prompt Corrective Action (PCA)

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- PCA is primarily to take appropriate corrective action on weak and troubled banks.
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- The RBI has put in place some trigger points to assess, monitor and control banks.
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- The trigger points are on the basis of CRAR (a metric to measure balance sheet strength), NPA and ROA (return on assets).
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- Based on each trigger point, the banks have to follow a mandatory action plan.
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- It prohibits them from undertaking fresh business activities such as opening branches, recruiting talent or lending to risky companies.
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- RBI could take discretionary action plans too apart from these.
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