

# GREAT LAKES



INSTITUTE OF MANAGEMENT, CHENNAI

## L'ATTITUDE 1305

### PRESENTS ARTHVRIDHI



## **ARTH BANK AND VRIDHI BANK**

The Manamai Stock Exchange, located at L'Attitude 13°05', is one of the buzzing stock exchanges in the region. The best investors are attracted towards the immense opportunities because of the transparent price discovery and stringent rules and regulations. The stock exchange is active with people trading money right from the opening bell till the end of day.

### **About Vridhi Bank:**

Vridhi Bank, in spite of its promising start, could not sustain its growth momentum. In 2008, it suffered heavily due to its aggressive lending which led to increasing NPAs. The bank has managed to keep its head just above the water and is on the look out for capital infusion through a strategic alliance.

### **About Arth Bank:**

Arth Bank is one of the leading banks in the area. Its strength remains in its large network of ATMs and branch offices, a huge and loyal customer base and well recognized brand. It is looking towards maintaining its market share through organic as well as inorganic growth. Arth bank has invested heavily, which has helped it increase its efficiency. Currently, the board of directors at Arth bank is on the lookout for potential acquisition targets at attractive prices which can increase shareholder value.

Arth bank has about 10% of the facilities located in the same region as the Vridhi bank. Management is looking at cutting the manpower cost by 5%. The acquisition can allow the bank to look at cutting its administrative cost which would enhance its bottom-line. It would also enable the bank to increase its market share.

	<b>Arth Bank</b>	<b>Vridhi Bank</b>
<b>No. of Branches</b>	150	45
<b>No. of ATMs</b>	475	85

The acquisition of Vridhi bank by Arth bank can bring about a lot of synergy to its existing operations. The valuation of Arth bank can increase as a result of this acquisition. The acquisition would allow Arth bank to tap into a large portion of Vridhi bank's customer base.

**The Arth bank's management is considering Vridhi bank as a potential target. The Arth management is looking at the financial statements (see exhibits). The management of Arth bank is posed with three questions-**

1. If it is an all equity acquisition, what would be the justified SWAP ratio? Kindly fortify your response.
2. What is the expected net synergy (in INR terms) they expect to derive from this merger in next three years?
3. Based on the synergy derived above, what should be the appropriate premium to pay?



**EXHIBIT 1: No. of shares outstanding**

<b>Arth bank</b>	<b>125 crores</b>
<b>Vridhi bank</b>	<b>100 crores</b>

**EXHIBIT 2: Vridhi Bank- Balance Sheet**

<b>Vridhi Bank</b>	<b>(All figures in INR crores)</b>		
Target Balance Sheet	<b>2007</b>	<b>2008</b>	<b>2009</b>
Total Share Capital	500	500	500
Reserves	1,500.00	1,181.69	1,201.39
<b>Owner's equity</b>	<b>2,000.00</b>	<b>1,681.69</b>	<b>1,701.39</b>
Deposits	35,000.00	48,000.00	55,000.00
Borrowings	145	555	400
<b>Liabilities</b>	<b>35,145.00</b>	<b>48,555.00</b>	<b>55,400.00</b>
<b>Total Liabilities &amp; Owner's equity</b>	<b>37,145.00</b>	<b>50,236.69</b>	<b>57,101.39</b>
<b>Assets</b>			
Cash & Balances with RBI	2,500.00	3,050.00	4,500.00
Balance with Banks, Money at Call	900	1,500.00	1000
Advances	20,500.00	30,450.00	40,000.00
Investments	12,286.62	13,200.00	10,000.00
Other Assets	958.38	2,036.69	1,601.39
<b>Total Assets</b>	<b>37,145.00</b>	<b>50,236.69</b>	<b>57,101.39</b>

**EXHIBIT 3: Vridhi Bank- Income Statement**

<b>Vridhi Bank</b>			
<b>Profit &amp; Loss account</b>	<b>(All figures in INR crore)</b>		
	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>Income</b>			
Interest Earned	3,500.00	3,700.00	5,300.00
Other Income	639.88	606.69	481.95
<b>Total Income</b>	<b>4,139.88</b>	<b>4,306.69</b>	<b>5,781.95</b>
<b>Expenditure</b>			
Interest expended	1,800.00	2,100.00	2,800.00
Employee Cost	540	550	800
Selling and Admin Expenses	192	350	450
Miscellaneous Expenses	694	490	295
Operating Expenses	500	940.00	1,118.25
Provisions & Contingencies	200	195	299
<b>Total Expenses</b>	<b>3,926.00</b>	<b>4,625.00</b>	<b>5,762.25</b>
<b>Net Profit for the Year</b>	<b>213.88</b>	<b>-318.31</b>	<b>19.70</b>

**EXHIBIT 4: Arth Bank- Balance Sheet**

<b>Arth Bank</b>	<b>(All figures in INR crore)</b>		
Suitor Balance sheet	<b>2007</b>	<b>2008</b>	<b>2009</b>
Total Share Capital	700	700	700
Reserves	3,000.00	5,369.69	7,689.64
<b>Owner's equity</b>	<b>3,700.00</b>	<b>6,069.69</b>	<b>8,389.64</b>
Deposits	85,000.00	97,000.00	115,000.00
Borrowings	400	800	1300
<b>Liabilities</b>	<b>85,400.00</b>	<b>97,800.00</b>	<b>116,300.00</b>
<b>Total Liabilities &amp; Owner's equity</b>	<b>89,100.00</b>	<b>103,869.69</b>	<b>124,689.64</b>
<b>Assets</b>			
Cash & Balances with RBI	12,100.00	14,400.00	18,000.00
Balance with Banks, Money at Call	9000	12,000.00	13000
Advances	39,300.00	43,000.00	57,300.00
Investments	24,800.00	28,700.00	30,389.64
Other Assets	3900	5,769.69	6,000.00
<b>Total Assets</b>	<b>89,100.00</b>	<b>103,869.69</b>	<b>124,689.64</b>

**EXHIBIT 5: Arth Bank- Income Statement**

<b>Arth Bank</b>			
<b>Profit &amp; Loss account</b>	<b>(All figures in INR crore)</b>		
	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>Income</b>			
Interest Earned	22,000.00	25,000.00	28,000.00
Other Income	639.88	606.69	481.95
<b>Total Income</b>	<b>22,639.88</b>	<b>25,606.69</b>	<b>28,481.95</b>
<b>Expenditure</b>			
Interest expended	18,000.00	20,000.00	22,000.00
Employee Cost	600	750	1000
Selling and Admin Expenses	222	387	567
Miscellaneous Expenses	694	430	395
Operating Expenses	677	1,400.00	1,700.00
Provisions & Contingencies	200	270	500
<b>Total Expenses</b>	<b>20,393.00</b>	<b>23,237.00</b>	<b>26,162.00</b>
<b>Net Profit for the Year</b>	<b>2,246.88</b>	<b>2,369.69</b>	<b>2,319.95</b>

**EXHIBIT 6: Average share/market values**

<b>Dates</b>	<b>Vridhi (Rs.)</b>	<b>Arth (Rs.)</b>	<b>Manamai Stock Exchange</b>
<b>Mar-07</b>	54	88	3500
<b>Jun-07</b>	50	104	3750
<b>Sep-07</b>	46	110	4000
<b>Dec-07</b>	48	126	4250
<b>Mar-08</b>	50	144	4500
<b>Jun-08</b>	46	178	4750
<b>Sep-08</b>	44	200	5000
<b>Dec-08</b>	42	210	5250
<b>Mar-09</b>	44	232	5500
<b>Jun-09</b>	36	254	5750
<b>Sep-09</b>	38	286	6000
<b>Dec-09</b>	38	314	6250