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## *ABOUT US*

WHITE BLACK LEGAL is an open access, peer-reviewed and refereed journal provided dedicated to express views on topical legal issues, thereby generating a cross current of ideas on emerging matters. This platform shall also ignite the initiative and desire of young law students to contribute in the field of law. The erudite response of legal luminaries shall be solicited to enable readers to explore challenges that lie before law makers, lawyers and the society at large, in the event of the ever changing social, economic and technological scenario.

With this thought, we hereby present to you

# HDFC LTD. AND HDFC BANK LTD. MERGER RATIONALE AND ITS IMPACT

AUTHORED BY - YASH PRATAP SINGH

## 1. Introduction

The successful completion of this merger of HDFC and HDFC Bank, effective from July 1, 2023, comes after receiving all necessary shareholder and regulatory approvals. The decision to merge, announced on April 4, 2022, was based on the shared vision of creating enhanced value for



Figure 1: HDFC Ltd. Logo



Figure 2: HDFC Bank Logo

stakeholders by leveraging the synergies between the two entities. HDFC Bank has become the 4<sup>th</sup> largest bank in the world after the massive merger with a market capitalization of \$178 billion<sup>1</sup>. Boasting a customer base surpassing Germany's population, the fresh HDFC Bank establishment accommodates a staggering 120 million customers, along with a network of over 8,300 branches and a workforce exceeding 177,000 employees<sup>2</sup>. It has surpassed huge banks like Citigroup and HSBC and ranked 4<sup>th</sup> and first Indian bank in the top 10 most valued banks<sup>3</sup>.

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<sup>1</sup> Joel Robello, *HDFC Merger to Create World's Fourth Largest Bank by Mkt Cap*, THE ECONOMIC TIMES, Jul. 1, 2023, <https://economictimes.indiatimes.com/industry/banking/finance/banking/hdfc-merger-to-create-worlds-fourth-largest-bank-by-mkt-cap/articleshow/101403184.cms?from=mdr> (last visited Aug 8, 2023).

<sup>2</sup> Binitha Jacob, *India's HDFC Bank Becomes 4th Largest In The World Following Massive Merger*, IBTIMES (Jul. 3, 2023), <https://www.ibtimes.com/indias-hdfc-bank-becomes-4th-largest-world-following-massive-merger-3703085> (last visited Aug 9, 2023).

<sup>3</sup> HDFC vaults into ranks of world's most valuable banks, THE HINDU BL, <https://www.thehindubusinessline.com/money-and-banking/hdfc-vaults-into-ranks-of-worlds-most-valuable-banks/article67025845.ece>. (last visited Aug 9, 2023).

Sashi Jagdishan, CEO of HDFC Bank in a press release said, *"This is a defining event in our journey and I'm confident that our combined strength will enable us to create a holistic ecosystem of financial services. We're truly happy to welcome the talented team of HDFC Ltd. into the HDFC Bank family. I believe our journey will be defined by agility, adaptability, and a relentless pursuit of excellence. As we navigate the path ahead, we will embrace challenges as opportunities, learn from our experiences, and strive to be the benchmark of success and integrity in the financial services industry."*<sup>4</sup>

HDFC Ltd.'s merger with the HDFC bank is one of the largest merger deals India has seen with a value of \$40 billion<sup>5</sup> and next to it is the Vodafone Idea merger which was valued at \$23 billion<sup>6</sup>.

The merger between HDFC Ltd. and HDFC Bank signifies a transformative step in India's financial landscape. By merging their strengths, these two stalwarts aim to deliver comprehensive financial services, foster economic growth, and create a harmonious and dynamic workplace for their employees.

## 1. Profiles of HDFC and HDFC Bank

**Housing Development Finance Corporation Ltd (HDFC)** stands as a non-banking deposit-taking financial firm, offering diverse housing finance solutions. These encompass loans for new homes, home improvements, extensions, land plots, properties, top-ups, education, and non-residential assets. HDFC extends insurance coverage including home, travel, motor, health, personal accident, retirement, property, marine, aviation, protection, savings, investments, and liability through its subsidiaries and associates. Additionally, it delivers rural housing finance, advisory services, portfolio management, mutual funds, property investment management, investment counselling, and real estate venture capital. Headquartered in India, HDFC maintains offices in Kuwait, Oman, Singapore, Dubai, and London, with its main base located in Mumbai, Maharashtra.<sup>7</sup>

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<sup>4</sup> HDFC Ltd. to merge into HDFC Bank effective July 1, 2023, (2023), [https://www.hdfcbank.com/content/bbp/repositories/723fb80a-2dde-42a3-9793-7ae1be57c87f/?path=/Footer/About%20Us/News%20Room/Press%20Release/Content/2023/pdf/Press\\_Release\\_HDFC\\_Ltd\\_to\\_merge\\_into\\_HDFC\\_Bank\\_effective\\_July\\_1\\_2023.pdf](https://www.hdfcbank.com/content/bbp/repositories/723fb80a-2dde-42a3-9793-7ae1be57c87f/?path=/Footer/About%20Us/News%20Room/Press%20Release/Content/2023/pdf/Press_Release_HDFC_Ltd_to_merge_into_HDFC_Bank_effective_July_1_2023.pdf). (last visited Aug 9, 2023).

<sup>5</sup> HDFC Bank at record high post HDFC-merger, among world's top 10 banks by value, ECONOMIC TIMES, <https://economictimes.indiatimes.com/markets/stocks/news/hdfc-bank-at-record-high-post-hdfc-merger-among-worlds-top-10-banks-by-value/articleshow/101452644.cms?from=mdr>.

<sup>6</sup> 5 biggest mergers & acquisitions in India: Reliance, Tata, Vodafone, Walmart – did their big bets pay off?, THE FINANCIAL TIMES, <https://www.financialexpress.com/market/5-biggest-mergers-amp-acquisitions-in-india-reliance-tata-vodafone-walmart-did-their-big-bets-pay-off/3156967/>.

<sup>7</sup> About Us, HDFC BANK, <https://www.hdfc.com/about-us/our-story> (last visited Aug 10, 2023).



Since its inception, HDFC has facilitated more than 3.8 million clients in acquiring their own homes, obtaining housing loan approvals exceeding Rs 3.73 trillion, and disbursing over Rs 3.02 trillion as of March 31, 2011. Its extensive network spans 351 locations nationwide, including 91 branches of its fully-owned distribution subsidiary, HDFC Sales Private Limited, catering to over 2,400 towns and cities. HDFC also serves Non-Resident Indians (NRIs) and Persons of Indian Origin (PIOs) with home loans and property advisory services in Dubai, London, Singapore, and other parts of the Middle East.<sup>8</sup>

As of January 3rd, 2023, the market price is Rs. 2650, the Dividend Yield stands at 1.15%, the P/E Ratio is 19.78, the EPS is 76.01, and the number of equity shares is 181.73 Crores.

Throughout its evolution, HDFC has grown into a financial behemoth, engaging in various financial sectors such as banking, life and non-life insurance, asset management, real estate venture capital, and more recently, education loans. Today, HDFC is recognized as one of India's best-managed companies, serving as a model for emerging nations with burgeoning housing finance markets. The corporation has undertaken advisory projects across Asia, Africa, and Eastern Europe, aiding in the establishment and development of housing finance organizations.

**HDFC Bank** was established in August 1994 under the name 'HDFC Bank Limited', headquartered in Mumbai, India. Commencing operations as a Scheduled Commercial Bank in January 1995, it emerged as one of the first to receive 'in-principal approval from the Reserve Bank of India (RBI) for establishing a private sector bank, in line with the RBI's efforts to liberalize the Indian Banking Industry in 1994. Presently, HDFC Bank operates a vast network comprising more than 1416 branches spanning 550 cities throughout India. These branches are interconnected in real-time through an online system. The bank also extends its services to customers in over 500 locations through Telephone Banking. Moreover, the bank has an extensive network of approximately 3382 networked ATMs across these cities. Leveraging its financial market experience, strong reputation, sizable shareholder base, and distinct consumer franchise, HDFC was aptly positioned to spearhead the establishment of a bank within the Indian landscape after the 1991 economic reforms.

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<sup>8</sup> Jash Chhabria, *Swap Ratio Determination for Merger: HDFC Ltd. & HDFC Bank*, SSRN JOURNAL (2023), <https://www.ssrn.com/abstract=4321520> (last visited Aug 10, 2023).

As of March 31, 2023, the Bank had an authorized share capital of ₹650 crore. The paid-up share capital of the Bank on that date was ₹557,97,42,786, consisting of 557,97,42,786 equity shares with a face value of ₹1/- each. Within the Bank's equity structure, the HDFC Group held approximately 20.87%, while the ADS Depositories held around 18.43% of the equity, which related to the Bank's American Depository Shares (ADS). Additionally, Foreign Institutional Investors (FIIs) owned about 26.30% of the equity, and the Bank had a total of 22,90,092 shareholders.<sup>9</sup>

The company's shares are listed on both the Bombay Stock Exchange Limited and The National Stock Exchange of India Limited. Furthermore, HDFC Bank's American Depository Shares (ADS) are listed on the New York Stock Exchange (NYSE) under the symbol 'HDB', while its Global Depository Receipts (GDRs) are listed on the Luxembourg Stock Exchange.<sup>10</sup>

The amalgamation of Centurion Bank of Punjab with HDFC Bank, approved by the Reserve Bank of India on May 23, 2008, marked a significant milestone. Under this scheme, shareholders of Centurion Bank of Punjab received 1 share of HDFC Bank for every 29 shares of Centurion Bank of Punjab. This merger resulted in a strengthened deposit base of approximately Rs. 1,22,000 crore and net advances of around Rs. 89,000 crore. The combined balance sheet size of the merged entity exceeded Rs. 1,63,000 crore. Notably, the amalgamation brought valuable additions to HDFC Bank, including an expanded branch network, broader geographical coverage, an increased customer base, and a larger pool of skilled personnel.<sup>11</sup>

As of January 3rd, 2023, the market price was at Rs. 1630, the Dividend Yield at 0.97%, the P/E Ratio at 21.31, the EPS at 66.8, and the number of equity shares were 272.3 Crores.<sup>12</sup>

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<sup>9</sup> About HDFC Bank, HDFC Bank, <https://www.hdfcbank.com/personal/about-us> (last visited Aug 10, 2023).

<sup>10</sup> Chhabria, *supra* note 8.

<sup>11</sup> About HDFC Bank, *supra* note 9.

<sup>12</sup> Chhabria, *supra* note 8.

## 2. Timeline of the Merger

Let's see the timeline of the whole merger with the help of a flowchart<sup>13</sup>:



## 3. Legal and Regulatory Framework

### 3.1 Companies Act

Chapter XV of the Companies Act, 2013 is dedicated to addressing matters concerning Compromise, Arrangements, and Amalgamations. The framework outlined within the Companies Act, 2013, encompasses the procedures for mergers as detailed in Sections 230 through 232. This merger process, operating under the Companies Act, 2013, is overseen by a judicial process led by the Tribunal as given under section 231. The initiation of this process involves the submission of an application to the National Company Law Tribunal (NCLT)<sup>14</sup>.

While the aforementioned provisions within the Companies Act, 2013 pertain to mergers and amalgamations involving two corporate entities, there exist distinct provisions governing the

<sup>13</sup> HDFC-HDFC Bank Merger: A look at the timeline of the move, CNBC TV18, <https://www.cnbc18.com/business/hdfc-hdfc-bank-merger-a-look-at-the-timeline-of-the-move-17089841.htm>.

<sup>14</sup> THE COMPANIES ACT, 2013, (2013), <https://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf> (last visited Aug 28, 2023).

merger and amalgamation of banking institutions. These provisions are issued by the Reserve Bank of India (RBI) and are referred to as RBI Amalgamation Directions. A pivotal guideline in the context of the merger and amalgamation of banking entities is outlined in Section 44A of the Banking Regulation Act (BR Act)<sup>15</sup>. It's noteworthy that these provisions in the BR Act are supplementary to, rather than in conflict with, the Companies Act, 2013. As a result, any compliance required under the BR Act complements the obligations established by the Companies Act, 2013, unless explicitly indicated otherwise.<sup>16</sup>

Furthermore, a notable aspect within this scenario pertains to the amalgamation of a Non-Banking Financial Company (NBFC) with a bank in India. For such scenarios, the regulatory provisions encompass Sections 230 through 232 of the Companies Act, 2013, in conjunction with the directives provided by the RBI's Amalgamation Directions. The RBI's directives concerning amalgamation encompass two primary scenarios: the first being the amalgamation of two private banks, and the second involving the merger of an NBFC with a private bank<sup>17</sup>.

The RBI's Amalgamation Directions stipulate that the voluntary amalgamation of an NBFC with a banking company is governed by Sections 232 to 234 of the Companies Act, 2013 and Chapter IV of the directions. According to these sections, the scheme of amalgamation necessitates approval from the Tribunal<sup>18</sup>.

## **3.2 Banking Regulation Act**

### **3.2.1 Shareholder and Board Approval**

Under the provisions of the Banking Regulation Act (BR Act), the amalgamation of a Non-Banking Financial Company (NBFC) with a bank mandates the approval of the respective Boards. This approval necessitates a two-thirds majority<sup>19</sup> of the total board strength, not limited to those present and voting, as mentioned in Chapter II of the directions. The responsibilities carried by non-executive and independent directors within the banking industry's unique nature also lead to

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<sup>15</sup> THE BANKING REGULATION ACT, 1949, (1949), <https://www.indiacode.nic.in/bitstream/123456789/1885/1/A194910.pdf> (last visited Aug 28, 2023).

<sup>16</sup> HDFC – HDFC Bank: Merger of Giant HDFC Twins!, M&A Lab (2022), [https://www.nishithdesai.com/fileadmin/user\\_upload/pdfs/Research\\_Papers/M&A\\_Lab\\_HDFC\\_Bank.pdf](https://www.nishithdesai.com/fileadmin/user_upload/pdfs/Research_Papers/M&A_Lab_HDFC_Bank.pdf) (last visited Aug 28, 2023).

<sup>17</sup> Master Direction – Amalgamation of Private Sector Banks, Directions, 2016, (2016), [https://rbi.org.in/Scripts/BS\\_ViewMasDirections.aspx?id=10364](https://rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=10364).

<sup>18</sup> Id.

<sup>19</sup> Id.

their engagement through a deed of covenants with the bank. Following the board's endorsement of the arrangement scheme, the next step involves presenting the scheme to the bank's shareholders. In Direction 7 of Chapter III, it is given that the scheme's approval requires a majority in number representing two-thirds in value of the shareholders present and voting<sup>20</sup>. Proxy voting is also an option available to shareholders during these resolutions.

It's crucial to note that the BR Act imposes a voting ceiling, disallowing any shareholder to exercise poll voting rights exceeding 10% of the total voting rights held by all shareholders<sup>21</sup>. This shareholder voting should only be convened after the approval of the draft scheme by the involved bank's boards, as given in Direction 8 of Chapter III<sup>22</sup>.

The considerations guiding the board's approval of the draft scheme encompass a range of factors, including the valuation at which the assets, liabilities, and reserves of the merged entity will be incorporated into the final company's books. The due diligence process conducted by the parties, determination of the swap ratio by independent valuers, compliance with RBI guidelines, and assessment of the impact on profitability and capital adequacy are all crucial elements in this assessment.<sup>23</sup> The respective boards of the two entities approved the Scheme on April 04, 2022<sup>24</sup>.

### **3.2.2 Approval by Central Bank**

Following the approvals from the board and shareholders, the amalgamation undergoes scrutiny from the Reserve Bank of India (RBI)<sup>25</sup>. HDFC Bank's disclosure on July 04, 2022, stated that the Scheme had received a no-objection letter from the RBI on the same date<sup>26</sup>.

After receiving approval from the board, the amalgamating entity, in this case, the bank, is obligated to provide specific documents to the RBI. These documents encompass a valuation report used to determine the share swap ratio, along with a detailed computation of the valuation. These materials enable the RBI to assess the proposed amalgamation and the potential for

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<sup>20</sup> Id.

<sup>21</sup> THE BANKING REGULATION ACT, 1949, supra note 15.

<sup>22</sup> Master Direction – Amalgamation of Private Sector Banks, Directions, 2016, supra note 17.

<sup>23</sup> Id.

<sup>24</sup> Disclosure under Regulation 30 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“Listing Regulations”)- Outcome of Board Meeting, (2022).

<sup>25</sup> Master Direction – Amalgamation of Private Sector Banks, Directions, 2016, supra note 17.

<sup>26</sup> Business Standard, HDFC Bank Receives No Objection Letter from RBI for Merger with HDFC, (2022), [https://www.business-standard.com/article/finance/hdfc-bank-receives-no-objection-letter-from-rbi-for-merger-with-hdfc-122070401339\\_1.html](https://www.business-standard.com/article/finance/hdfc-bank-receives-no-objection-letter-from-rbi-for-merger-with-hdfc-122070401339_1.html) (last visited Aug 28, 2023).

enhancing value. It was interesting to note that the RBI's issuance of the No-Objection Letter diverges from the typical approval process outlined in the RBI Amalgamation Directions. Instead of a direct approval, the RBI's letter to HDFC Bank includes specific conditions or conditionalities, as reported in the public domain.

### **3.3 SEBI and Stock Exchanges**

The regulations outlined by the Listing Regulations<sup>27</sup> dictate that any publicly listed entities engaging in a scheme of amalgamation must initially submit the draft scheme to the relevant stock exchanges before proceeding with the submission to the Tribunal (as per the process laid down under CA 2013). This submission to the stock exchanges is aimed at obtaining an observation letter or a no-objection letter from these exchanges<sup>28</sup>. Given that both HDFC Limited and HDFC Bank are entities listed on stock exchanges, seeking approval from the pertinent stock exchanges was an essential step. However, it's noteworthy that this requirement does not apply to schemes solely focused on the merger of a wholly-owned subsidiary with the parent company<sup>29</sup>. Importantly, HDFC Bank received the observation letter with 'no-adverse observations' and 'no-objection' from BSE and NSE respectively on July 02, 2022<sup>30</sup>.

By CA 2013, the scheme of amalgamation is required to be presented before SEBI<sup>31</sup>. SEBI is then allotted a 30-day window from the receipt of notice of the meeting of creditors or class of creditors, or members of a class of members, as mandated by the Tribunal, to provide any representations or comments. Should SEBI fail to do so within this timeframe, it is assumed that SEBI has no objections to the proposal.

Following the reception of the draft scheme of arrangement and associated documents as per Regulation 37(1) of the Listing Regulations<sup>32</sup>, the relevant stock exchange forwards these

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<sup>27</sup> Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, (2015), [https://www.sebi.gov.in/legal/regulations/apr-2022/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-regulations-2015-last-amended-on-april-25-2022-\\_58418.html](https://www.sebi.gov.in/legal/regulations/apr-2022/securities-and-exchange-board-of-india-listing-obligations-and-disclosure-requirements-regulations-2015-last-amended-on-april-25-2022-_58418.html) (last visited Aug 28, 2023).

<sup>28</sup> Id.

<sup>29</sup> Circular on Schemes of Arrangement by Listed Entities and (ii) Relaxation under Sub-rule (7) of rule 19 of the Securities Contracts (Regulation) Rules, 1957, (2017), [https://www.sebi.gov.in/legal/circulars/mar-2017/circular-on-schemes-of-arrangement-by-listed-entities-and-ii-relaxation-under-sub-rule-7-of-rule-19-of-the-securities-contracts-regulation-rules-1957\\_34352.html](https://www.sebi.gov.in/legal/circulars/mar-2017/circular-on-schemes-of-arrangement-by-listed-entities-and-ii-relaxation-under-sub-rule-7-of-rule-19-of-the-securities-contracts-regulation-rules-1957_34352.html) (last visited Aug 28, 2023).

<sup>30</sup> Standard, supra note 26.

<sup>31</sup> THE COMPANIES ACT, 2013, supra note 14.

<sup>32</sup> Disclosure under Regulation 30 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("Listing Regulations")- Outcome of Board Meeting, supra note 24.

materials to SEBI for approval. Upon the issuance of the no-objection letter by the relevant stock exchanges, SEBI undertakes the evaluation of the draft scheme and furnishes its comments within 30 days. This period is measured from the later of these dates:

- The date of receiving a satisfactory reply on clarifications, if any were sought by SEBI from the listed entity.
- The date of receiving an opinion from an independent chartered accountant, if solicited by SEBI.
- The date of receiving the 'no-objection' letter from the relevant stock exchanges.

Subsequently, on April 26, 2023, BSE and NSE granted permission for the transfer of Non-Convertible Debentures (NCDs) from HDFC Ltd. to HDFC Bank. The final and essential approval from SEBI was eventually granted on May 24, 2023<sup>33</sup>.

### **3.4 Competition Commission on India**

The Competition Act<sup>34</sup>, in conjunction with the CCI (Procedure regarding the transaction of business relating to combinations) Regulations, 2011<sup>35</sup>, establishes a prohibition against individuals or enterprises engaging in a 'combination' that triggers or is likely to trigger an 'appreciable adverse effect on competition' ("AAEC") within the relevant Indian market. Such a combination is deemed void.

Under the framework of the Competition Act, a 'combination' includes a merger or amalgamation in which the resulting entity, following the merger, possesses assets either in India or outside India that surpass the financial thresholds stipulated by the Competition Act.

By Section 5(c)(ii) of the Competition Act, the amalgamation of enterprises is classified as a 'combination' if any amalgamation results in the group that remains post-amalgamation having:

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<sup>33</sup> HDFC-HDFC Bank Merger: A look at the timeline of the move, CNBC TV18, <https://www.cnbc18.com/business/hdfc-hdfc-bank-merger-a-look-at-the-timeline-of-the-move-17089841.htm>.

<sup>34</sup> THE COMPETITION ACT, 2002, (2003), <https://www.cci.gov.in/images/legalframeworkact/en/the-competition-act-20021652103427.pdf>.

<sup>35</sup> The Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011, (2009), <https://www.cci.gov.in/images/combolegalframeworkregulation/en/cci-procedure-in-regard-to-the-transaction-of-business-relating-to-combinations-regulations-2011.pdf>.

- (a) Assets in India with a value exceeding INR 4,000 Crores (approximately USD 500 Million) or a turnover exceeding INR 12,000 Crores (approximately USD 1.5 Billion), or
- (b) In India or internationally, an aggregate value of assets exceeding USD 2 Billion (including at least INR 500 Crores, approximately USD 62.5 Million, in India), or a turnover exceeding USD 6 Billion (including at least INR 1,500 Crores, approximately USD 187.5 Million, in India).<sup>36</sup>

Consequently, the Deal was formally notified to the Competition Commission of India (CCI) in June 2022 by the involved parties and approved by the CCI on August 13, 2022<sup>37</sup>.

### **3.5 Insurance Regulatory and Development Authority of India (IRDAI)**

HDFC's subsidiaries, HDFC Life Insurance and HDFC General Insurance were owned in part by HDFC Limited. Before any merger, HDFC Limited held significant stakes in both.

The Insurance Act<sup>38</sup>, along with various IRDAI regulations, imposes specific rules. Approval from the Insurance Regulatory and Development Authority of India (IRDAI) is needed in scenarios involving the acquisition or transfer of shares in insurance companies. These rules apply to listed insurance companies. The Scheme involves HDFC Bank acquiring ownership of HDFC's insurance subsidiaries. This necessitates obtaining prior approvals from IRDAI.

After the merger, HDFC Bank is expected to hold substantial stakes in these insurers. The Reserve Bank of India (RBI) is cautious about banking companies holding more than 30% of insurance companies, due to the capital-intensive nature of the insurance sector. Consequently, the RBI has set caps on banks' ownership in insurers, with a recent directive limiting stakes to 20%<sup>39</sup>.

### **3.6 Takeover Code**

It's important to note that Regulation 10(d) of the Takeover Code in India plays a crucial role in determining whether a merger or acquisition triggers an open offer requirement. This regulation specifically pertains to acquisitions that result from a scheme of arrangement involving the target

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<sup>36</sup> THE COMPETITION ACT, 2002, supra note 34.

<sup>37</sup> HDFC-HDFC Bank Merger: A look at the timeline of the move, supra note 33.

<sup>38</sup> Insurance Act, 1938, (1938), <http://indiacode.nic.in/handle/123456789/2304> (last visited Sep 3, 2023).

<sup>39</sup> RBI restricting banks from raising stakes in insurance firms: Report, mint (2021), <https://www.livemint.com/insurance/news/rbi-restricting-banks-from-raising-stakes-in-insurance-firms-report-11614684604707.html> (last visited Sep 3, 2023).



company, either as a transferor or transferee, or as a part of a reconstruction process, which includes amalgamation, merger, or demerger. These actions must be carried out under an order issued by a court or a competent authority under any applicable Indian or foreign law or regulation<sup>40</sup>.

This is a merger under the Companies Act 2013, it falls within the scope of Regulation 10(d). This means that such a merger, when authorized by a court or a competent authority, is exempt from triggering an open offer obligation under the Takeover Code. This exemption is crucial because it provides legal clarity and ensures that certain corporate restructuring activities are not subject to the open offer requirement, which would otherwise be a significant financial burden on the merging entities.

### **3.7 Other**

According to Regulation 30(1) of the Listing Regulations, every listed company must inform the stock exchange about significant events or information. This helps shareholders and the public understand the company's status and prevents misleading trading in its stocks<sup>41</sup>. On April 4, 2022, HDFC Limited and HDFC Bank promptly informed the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) about their merger plan. They did this right after their board meeting approved it on the same day<sup>42</sup>.

Following Regulation 37(1) of the Listing Regulations, listed companies must make initial disclosures to the stock exchange to obtain a no-objection letter or no-observation letter. Afterwards, they follow the process outlined in the Companies Act of 2013, particularly Sections 230 to 232. In the event of a merger, listed companies must provide specific details as per Regulation 69(2) to the relevant stock exchanges where their securities are traded.

A company seeking a merger must submit various documents, such as a draft merger plan, a valuation report, and recommendations from the audit committee. They must ensure that their

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<sup>40</sup> SEBI | Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, (2011), [https://www.sebi.gov.in/legal/regulations/apr-2019/securities-and-exchange-board-of-india-substantial-acquisition-of-shares-and-takeovers-regulations-2011-last-amended-on-july-29-2019-\\_40714.html](https://www.sebi.gov.in/legal/regulations/apr-2019/securities-and-exchange-board-of-india-substantial-acquisition-of-shares-and-takeovers-regulations-2011-last-amended-on-july-29-2019-_40714.html) (last visited Sep 3, 2023).

<sup>41</sup> Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, *supra* note 27.

<sup>42</sup> Disclosure under Regulation 30 of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“Listing Regulations”)- Outcome of Board Meeting, *supra* note 24.

accounting complies with government standards. Independent directors also need to provide their input. Furthermore, the company must declare any previous defaults on debt obligations, as mentioned in various SEBI circulars. Additionally, the company must obtain a no-objection certificate (NOC) from lending scheduled commercial banks, financial institutions, or debenture trustees. Given that HDFC Bank issued debt securities on NSE INX in 2021, they were obliged to disclose any material or price-sensitive events regarding these securities, following the Framework for Listing Debt Securities.<sup>43</sup>

## **4. Merger Rationale and Benefits**

The merger aims to harness the complementary strengths of both HDFC Bank and HDFC Ltd., resulting in a comprehensive suite of financial services, spanning banking, insurance, and mutual funds through its subsidiaries. The combined entity is poised to deliver increased scale, a broader product offering, balance sheet resilience, and operational synergies. Through this strategic amalgamation, the institutions aim to provide enriched value to their respective customers, employees, and shareholders.

### **5.1 Regulation of NBFCs**

After the NBFC crisis in 2018 and 2019, RBI has been tightening its grip over the NBFCs. Infrastructure Leasing & Financial Services Limited (IL&FS) was a large infrastructure finance company in India. In September 2018, IL&FS defaulted on its debt obligations. The Indian government intervened to rescue IL&FS by setting up a new board of directors and injecting capital into the company. The government also created a new regulatory framework for NBFCs to try to prevent similar crises from happening in the future.<sup>44</sup>

Dewan Housing Finance Corporation Limited (DHFL) was a non-banking financial company (NBFC) in India. It was the largest housing finance company in India by assets until it was overtaken by HDFC Bank in 2018. DHFL's troubles began in September 2018, after a Cobra Post sting operation alleged that the company had siphoned off money to related entities. Credit rating agencies started downgrading their paper in June 2019. The company also missed interest

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<sup>43</sup> HDFC – HDFC Bank: Merger of Giant HDFC Twins!, supra note 16.

<sup>44</sup> Manoj Kumar & Promit Mukherjee Reuters, Govt's Rescue of IL&FS May Spell Major Losses for Lenders, mint (2018), <https://www.livemint.com/Companies/gwdinCb9rHtAvF8ZbR45GN/Indias-rescue-of-ILFS-may-spell-major-losses-for-lenders.html> (last visited Aug 17, 2023).

payments on its debt obligations.<sup>45</sup> In April 2020, DHFL was placed under bankruptcy proceedings by the National Company Law Tribunal (NCLT). The company was eventually acquired by Piramal Capital and Housing Finance in July 2021.<sup>46</sup>

In the Indian economic landscape, standalone NBFCs face limited incentives. Moreover, the RBI has been progressively tightening regulations for these entities, making it challenging for prominent NBFCs to adhere to these rules. Since these regulations closely resemble those governing banks, it becomes logical for a housing finance company to merge with its larger banking counterpart.<sup>47</sup> The amalgamation of HDFC and HDFC Bank is perceived as a strategic step that offers regulatory benefits to both entities. Over recent years, regulations governing banks and NBFCs (Non-Banking Financial Companies) have been aligned, simplifying the process of making merger choices.

## 5.2 Bigger Loans

The merger between HDFC Bank and HDFC Ltd marks a significant step forward in the financial landscape, fostering a powerful synergy that propels the loan book growth while presenting certain challenges in terms of deposit growth. However, it's notable that the growth in the deposit book post-merger remains confined to single digits. This is attributed to the nature of HDFC Ltd as a deposit-taking Housing Finance Company (HFC) which predominantly relies on Term Deposits spanning 3 to 5 years and various forms of borrowings such as Non-Convertible Debentures (NCDs) and Commercial Papers (CPs) and lacks Current and Savings Account (CASA) deposits similar to traditional banks.

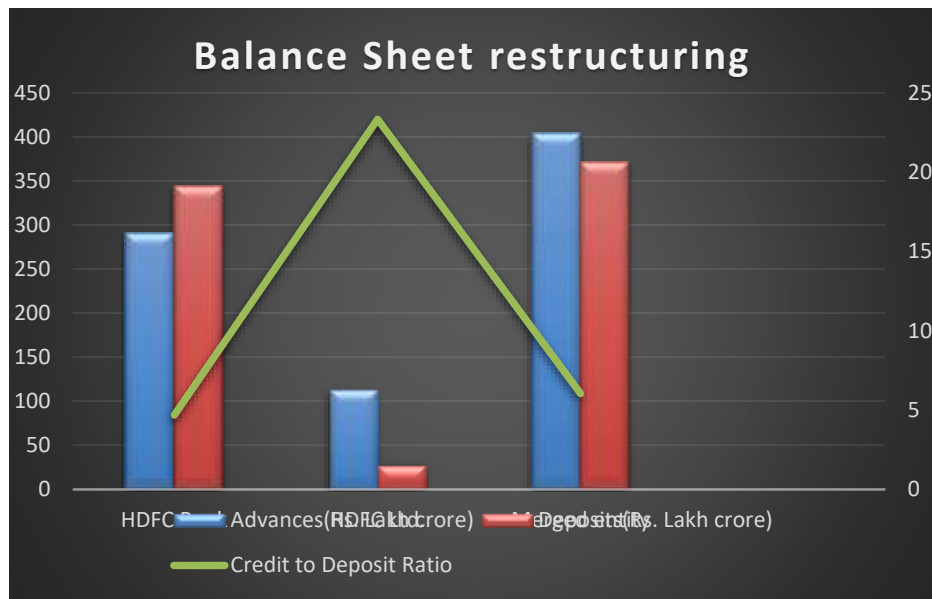
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<sup>45</sup> DEWAN HOUSING FINANCE CORPORATION LIMITED- THE ANATOMY OF INDIA'S BIGGEST FINANCIAL SCAM, Cobrapost, <https://cobrapost.com/blog/biggest-financial-scam/1373> (last visited Aug 17, 2023).

<sup>46</sup> NCLT approves Piramal offer to acquire DHFL with conditions, VCCircle, <https://www.vccircle.com/nclt-approves-piramal-offer-to-acquire-dhfl-with-conditions> (last visited Aug 17, 2023).

<sup>47</sup> After the storm: The Hindu Editorial on tightening scrutiny of large NBFCs, The Hindu, Jan. 25, 2021, <https://www.thehindu.com/opinion/editorial/after-the-storm-the-hindu-editorial-on-tightening-scrutiny-of-large-nbfcs/article33651448.ece> (last visited Aug 17, 2023).

Figure 3 Balance sheet restructuring <sup>48</sup>



Consequently, the Credit to the credit-to-deposit ratio (CD ratio) post-merger experiences an elevation from 84% to 109%, a shift that reflects the intricacies of the merger. The management acknowledges that this increase is inevitable on the first day of the merger; however, the focus lies on the subsequent trajectory. This strategic move calls for a meticulous restructuring of the balance sheet. The primary focus of this endeavour is the establishment of a robust deposit base, achieved through a deliberate pursuit of higher incremental growth in deposits compared to credit. To achieve this, the bank is channelling its efforts into attaining a quarter-on-quarter deposit growth rate of 1.2%, while maintaining a credit growth rate of 0.7% QoQ.

By adopting this approach, the incremental CD ratio is expected to remain within a range that is lower than the bank's existing level. This calibrated approach enables the bank to gradually bridge the gap and converge towards the current CD ratio of HDFC Bank. This progressive strategy encapsulates the bank's commitment to maintaining a stable financial equilibrium while navigating the complexities that arise from the merger.

In essence, the HDFC Bank and HDFC Ltd merger represents a symbiotic relationship that is poised to enhance the loan book, address challenges in deposit growth, and ultimately solidify the financial position of the merged entity. Through a combination of strategic foresight and

<sup>48</sup> Latha Venkatesh, HDFC Bank Will Have to Compete in the Market for Deposits, Says Former RBI Deputy Governor SS Mundra, cnbctv18.com (2023), <https://www.cnbctv18.com/finance/hdfc-bank-will-have-to-compete-in-the-market-for-deposits-says-former-rbi-deputy-governor-ss-mundra-17127931.htm> (last visited Aug 17, 2023).

incremental adjustments, the bank is orchestrating a measured transformation that aligns with its long-term vision.

### **5.3 Bigger Customer Base<sup>49</sup>**

One interesting aspect is how HDFC Ltd is teaming up with HDFC Bank. This is a big deal because it means HDFC Ltd can tap into HDFC Bank's vast network. Right now, HDFC Bank has an impressive 6,500 branches spread out all over the place. But here's the thing – not all of these branches are currently offering home loans and the reason for that is they prefer doing face-to-face meetings with borrowers, and some places are just too far to make that happen. When HDFC Ltd and HDFC Bank become one, this rule is going to change as now home loans can be offered across a much wider area.

HDFC Bank can learn from HDFC Ltd's extensive 45-year experience in the home loan arena. The company has truly mastered this field, enabling the provision of loans at a more economical rate. Adding to this, the astute strategy employed is evident in the company's low 8.1% cost relative to generated revenue. As HDFC Bank commences the adoption of these methodologies, the potential exists for further reduction in its operational expenditures.

A significant number of individuals familiar with HDFC Ltd presently abstain from utilizing HDFC Bank's services – this accounts for approximately 70% of the group! However, the proposition is this: upon engaging with these individuals, a considerable portion may opt to explore HDFC Bank's offerings. Furthermore, within HDFC Bank's customer base, merely 8% hold home loans, with a mere 2% originating from HDFC Ltd's end. This situation presents an outstanding opportunity to diversify the spectrum of services extended to a wide array of customers.

Moreover, consider this confidential insight: following the merger, HDFC Bank will possess the capability to introduce a selection of sophisticated services. Think of it as acquiring an advanced toolkit, enabling the provision of multifaceted financial solutions – far surpassing the potential of a stand-alone home loan company.

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<sup>49</sup> Keki Mistry lists the benefits of HDFC-HDFC Bank merger, says will start meeting investors, The Economic Times, May 4, 2022, <https://economictimes.indiatimes.com/markets/expert-view/keki-mistry-lists-the-benefits-of-hdfc-hdfc-bank-merger-says-will-start-meeting-investors/articleshow/91305691.cms?from=mdr> (last visited Aug 10, 2023).

To summarize, this merger entails more than just collaboration – it encompasses extending outreach, disseminating our expertise in home loans, broadening the scope of service offerings, and instigating a plethora of exhilarating prospects for all stakeholders. Visualize the creation of a larger team equipped with refined skills and advanced tools to pave the way for an enhanced financial future for all involved.

#### **5.4 Holding company discount<sup>50</sup>**

Imagine you have a big piggy bank called HDFC. Inside that piggy bank, you have two important things. One is a special business where people borrow money to buy homes (that's the mortgage business), and the other is the money you've invested in other companies.

Now, the money you invested in those other companies has grown a lot over time. It's like you put in a little bit of money, and it turned into a lot more. But when people look at your piggy bank's value, they don't give you full credit for all that extra grown-up money. They kind of reduce its value because your piggy bank is like a boss overseeing all these other companies, and they think that's not as valuable. This reduction in value is called a "holding company discount," and it's about 40%.

So, even though your piggy bank's extra grown-up money from those other companies is around Rs 1,60,000 crore, the market only counts around Rs 95,000 crore of that in the piggy bank's value.

Now, here's where the merger comes into play. When your piggy bank (HDFC) joins forces with another piggy bank (HDFC Bank), that "holding company discount" goes away. It's like people suddenly realize that your piggy bank being in charge of all these companies is a good thing. This makes your piggy bank's value go up by about Rs 60,000-65,000 crore again.

#### **5.5 More Foreign Investment<sup>51</sup>**

Imagine you have a pie, and you own 21% of that pie. Right now, people think that the whole pie is owned by friends from outside the country. But when you get inside the pie (like a magical pie-house), you find out that only a part of it, around 69%, is owned by your foreign friends. The rest, about 31%, is owned by friends who live nearby. So, 69% of your 21% piece of pie is seen as

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<sup>50</sup> Id.

<sup>51</sup> Id.

foreign, and the remaining 31% is seen as local. This means that the part foreigners can own in the pie will go up by about 10%. It's like more of your foreign friends get to have a slice. And here's a cool thing about the pie's growth (which is like the bank's business): because of this pie-house situation, the time the pie can stay fresh and delicious goes up. This means the pie can grow bigger and better, which helps the business grow faster. All these cool things happening when the pie joins forces are called "synergies" of the merger. It's like all the good stuff that happens when the pie and the pie house become one big pie house! And there is a similar situation concerning the HDFC bank and HDFC.

## **5. Conclusion**

HDFC and HDFC merger was announced back in April 2022 and the merger became effective on June 1 with shares being allotted to the people on July 13. HDFC and HDFC Bank merger has given birth to new a behemoth company which we can already see in the stats above and this is going to be beneficial overall for the customers, nation, and other people as well, making sure that its management maintains the same effectiveness. Now HDFC can give bigger loans so it can fund bigger and better projects and it will be the first bank in India to compete with international giants like JP Morgan, Morgan Stanley, Bank of America, ICBCL, etc. but that too only when they hit the targets they have decided and remove the hurdles that this merger has created, or they were already facing. This comes at a time when the Indian economy is growing steadily and needs institutions like this because the growth of these institutions is indirectly the growth of India, and we need more of them in all the sectors.