Concerns on Bank Merger

Why in news?

\n\n

Ministry of Finance has decided to merge three public sector banks recently.

\n\n

How was the evolution of Indian banks since nationalisation?

\n\n

\n
- Indian banking has grown and exhibited much diversity in size, content and structure after nationalisation of banks.
\n
- It witnessed the rise of several diverse banking institutions in the form of PSBs, regional rural banks, private banks, foreign banks, cooperative urban banks, cooperative rural banks, small payments banks, small finance banks and NBFCs.
\n
- Such diversity and effective regulatory oversight contained the contagion effect of the decade-old global recession on the Indian economy.
\n
- Business correspondents support the financial inclusion efforts of banks.
\n
- However, the **Narasimhan Committee** formed in 1994 argued for six large globally competitive banks and preferred closing the weak banks to merging them with strong ones.
\n
- There have been 39 mergers and takeovers during the post-nationalisation period, which includes the SBI merger.
\n
- This makes it very important on part of the government to draw lessons from all these mergers.
\n

\n\n

What are the effects of merger?

\n\n

\n
- A study was done on the pre and post-merger comparisons of profitability with the year of merger as base year in the case of SBI, IOB, BoB, PNB, IDBI and OBC.
\n
- It reveals that net profit to total income, net profit to interest income, net profit to total assets and net profit to net worth declined for all except PNB and BoB.
\n
- The exception was partly due to the period of merger, when the capital regulations post-Basel did not hit them.
\n
- Also, human resource and cultural issues have impeded the success of mergers across periods and nations.
\n
- It is therefore becoming important for big banks to think twice before turning into unwieldy conglomerates, since basic banking and customer services cannot be compromised.
\n
- All banks reduced their presence in rural and semi-urban, non-profitable centres during the post-liberalisation period in 1991.
\n
- The merger of State banks with its associates resulted in the closure of about 5,000 branches.
\n
- It thus effectively curtailed the plan to reach the unbanked poor.
\n

\n\n

What should the government do?

\n\n

\n
- Jan Dhan Yojana served as an effective tool to increase the financial inclusion agenda.
\n
- Establishment India Post Payments Bank also took banking services to the doorsteps of the least banked.
\n
- Even then, former RBI Governors cautioned the government against seeing consolidation as a panacea for the ills of the banking system.
\n

- There were legal and regulatory measures to address the NPA issues (non-performing asset) through market-based resolution plan in the form of insolvency (IBC) code.
\n
- Efforts were also taken to put 11 banks under surveillance via prompt corrective action plan to de-stress the banking sector.
\n
- However, the government has put together another merger, even before the results of the PCA were known.
\n
- This made the RBI's Financial Stability Report to warn against complacency, even though it has estimated healthy economic growth of over 7.5% for 2018.
\n
- Government on its part would do well to start infrastructure **development banks** to fund infrastructure projects and relieve PSBs of this task.
\n
- Experience has demonstrated that PSBs are not right channel for that job as it involves funding long-term projects with their short term resources.
\n
- It would also reduce their risk weighted assets and reducing the possibility of their assets turning into NPA's.
\n
- Universal banking did enough damage with banks selling more third-party products, eyeing hefty commissions, instead of focussing on core banking operations.
\n
- To improve its own stock, the government would do well to concentrate on improving governance in PSBs through bank board bureau and should pledge not to interfere in loan sanctions.
\n
- It could also move a resolution in Parliament that no party would indulge in loan write-offs either for the farm or other sectors unless the areas are affected by severe natural calamities.
\n

\n\n

What lies ahead?

\n\n

\n
- While past accomplishments are no guarantee to future success, past failures can serve as good foundation for enduring success.
\n
- Higher capital allocation with or without Basel-III alone cannot prevent bank

failures that are otherwise triggered by systems, people and processes.
\n
- Hence, toying with the financial sector with mergers looks faulty, unwise and untimely.
\n

\n\n

Source: Business Line

\n

