Fiscal Measures - Economic Slowdown

Why in news?

Finance Minister recently announced a set of measures aimed at reviving the economy and boosting investor sentiment. Click here to know more.

What are the key announcements?

- The government announced that it would frontload the release of Rs 70,000 crore to state-owned banks for recapitalisation.
- It was also decided to link the interest rate on loans to the RBI’s key policy rate, the repo rate.
- It was also promised that bankers would be protected in cases where bonafide decisions are taken by them while lending.

How effective will this be?

- The release of growth capital for banks should help lenders to plan their asset growth better.
- However, differences might arise among government, central bank and banks, on linking the interest rate on loans to the repo rate.
- The rationale for pricing loans based on what is essentially an overnight borrowing rate is not clear, especially in the context of funding costs for banks.
- [Ideally, such a benchmarking should be to liquid bonds or securities and across different average maturities or tenures (3-, 6-months and one-year) like the London Inter-Bank Offered Rate or Libor.]
- Also, it may be too optimistic to expect bankers to push loan growth in the absence of more credible assurances of protection from investigative agencies.
- Essentially, some of the measures unveiled for the financial sector may prove only to be short-term heal.

What is the way forward?

- India’s banking industry, dominated by PSU lenders, will be competitive, more efficient and profitable only if there is a structural design change.
- This should feature operational independence, empowered bank boards, better governance standards and quality of lending.

- Besides, it is favourable if there is a government shareholder which acts like a sovereign wealth fund.
- This will have to be accompanied by stable government and regulatory policies.

Source: Indian Express