PSBs Recapitalisation Plan

Why in news?

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- The government recently announced the details of the earlier said Rs. 2.1 lakh crore recapitalisation plan for public sector banks.
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- Click here to know more on the plan.
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What are the provisions?

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- **Package** - The recapitalisation package will be spread across current financial year 2017-18 and the next year 2018-19.
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- The government will infuse around Rs 88,000 crore into 20 public sector banks.
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- These banks account for more than 80% of the bad loans.
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- **Themes** - The plan includes a reforms package across six themes.
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- They are:
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1. customer responsiveness
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2. responsible banking
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3. credit offtake
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4. PSBs as Udyami Mitra (friends of entrepreneurs)
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5. deepening financial inclusion and digitalisation
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6. developing personnel for brand PSB
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- The whole-time directors of the PSBs would be assigned theme-wise reforms to oversee.
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- Their performance on the themes would be evaluated by the boards of the banks.
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- **Differential approach** - The recapitalisation package would follow a differentiated approach for banks.
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- The capital infusion for the PSBs would be dependent on banks' performance.
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- Accordingly, the government will give more money to the weakest ones.
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- These are the 11 lenders under the Reserve Bank of India's *Prompt Corrective Action* (PCA).
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- In financial year 2017-18, PCA banks would get around Rs. 50, 000 crore.
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- The comparatively healthier non-PCA banks would get around Rs. 35,000 crore.
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- **Recapitalisation bonds** - The capital infusion will be done partly by *recapitalisation bonds* and partly by budgetary support.
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- The bonds are to have a maturity period of 10-15 years and would be issued in six different slots.
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- They will not have a statutory liquidity ratio (SLR) requirement and would be non-tradeable.
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- The government has set strict terms for issuing the recapitalisation bonds to PSBs.
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- The terms include :
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i. creating a stressed asset management vertical

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ii. tying up with agencies for specialised monitoring of loans above Rs 2.5 billion

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iii. strict surveillance on big loan defaulters

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iv. appointing a whole-time director for monitoring reforms every quarter

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Will there be a fiscal impact?

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- There are apprehensions that the recapitalisation bonds would affect the fiscal consolidation efforts by the government.
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- The government however assured that it would not have any substantial impact on the fiscal deficit.
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- This is because the recapitalisation bonds would be "cash neutral" (does not need net cash for a transaction).
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- The fiscal deficit will be impacted only by the interest cost on the bonds that the government pays every year.
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What are the benefits?

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- The recapitalisation package will create an incremental **lending capacity** with the banks.
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- This is expected to catalyze the revival of the capital investment cycle in the economy.
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- Banks will now be sufficiently capitalised to maintain **regulatory capital requirements** and also to lead growth.
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- Banks would have to subject themselves to reform, become more professional, and do prudent and clean lending.
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- The government would bring out a report card on compliance of these measures.
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Source: The Hindu, Business Standard

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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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- RBI could take discretionary action plans too apart from these.
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- RBI has initiated prompt corrective action (PCA) in as many as 11 PSBs.
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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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Recapitalisation bonds

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- The idea is to borrow from the banks themselves and boost the weaker banks' capital, without immediate demand for direct government budgetary support.
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- Banks will subscribe to these bonds as part of their investment portfolio.
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- They will use the excess deposits they acquired from the recent demonetisation drive to invest in the bonds.
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- The money raised by the government will then be used to infuse fresh equity into weaker banks.
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