



Recapitalization of Banks

Description

Background :-

Since the government has a major stake in public sector banks it injected capital through Recapitalization bonds, raised equity through market and budgetary allocation to reduce the increasing problem of bad debt. In 2017, Government of India announced that it is going to infuse Rs 2.11 lakh crores in the Public Sector banks over 2 years through recapitalization to solve the banking financial crisis.

Current Situation :-

As the Budget document of FY20 showed no recapitalization drive, the State owned banks are expected to start 2019-20 on a strong financial footing.

- As per the current scenarios the NPAs show a negative trend in FY19 and have reduced by Rs 23,860 crore between April-September 2018, while they recovered Rs 60,726 crore. The recovery is more than double the amount recovered in the corresponding period last year.
- In its bi-annual Financial Stability Report (FSR), the RBI said that the NPAs in the banking sector may reduce from 10.8 percent (registered in September 2018) to 10.3 percent by March 2019 and further to 10.2 percent by September 2019. The ratio was 11.5 percent at the end of March 2018.
- Three banks — Bank of Maharashtra, Bank of India and Oriental Bank of Commerce — were brought out of the PCA restrictions on January 31 after their Q3 results met with the stipulated requirement to function as a normal bank.

Government's proposition for 2018-19 :-

- The government planned to provide Rs 88,139 crore for Public Sector Banks to boost lending and revive growth. Out of this mammoth amount, Rs 80,000 crore would be from recapitalization bonds and rest Rs 8,139 crore would be from budgetary allocation. This is



part of the Rs.2.11 lakh crore bank recapitalization plan announced in October 2017 last year.

- The government also planned to bring banking sectors reforms along with this recapitalization. This includes scrutiny of all loans above Rs 250 crore by specialized monitoring agencies and requirement to have a stressed asset management vertical to ensure stringent recovery follow-up.

Need for Recapitalization :-

- Lack of dynamism: There are 21 public sector banks in India which account for 70 per cent of the total banking assets in India. The lack of efficient management at the bank level and the inefficient control systems of the Finance ministry which, hinder the judicious flow of funds and are unable to prevent the conversion of an account into NPA, keeps these banks starved for funds and crying for more and more capital infusion every now and then.
- Non-Performing Loans: As of June 2017, the NPA's of the banking system were as high as 10.2% of the loans advanced by the banks, this ratio increased to 12.2% by the end of September 2017. The volume of bad debt hit 9.46 trillion rupees at the end of half of financial year 2017. Out of this the public sector bank's share was a whopping 8.25 trillion rupees. This resulted in limited lending capacity of banks and decreased the credit creation. It was noted that the credit growth was just 5.1% in 2016-2017 which is the lowest since 1951.
- Banking scams leading to consistent increase of NPAs: Big commercial finances like Kingfisher of Vijay Mallya, Gitanjali Gems & 23 other companies associated to Nirav Modi and Mehul Choksi, Rotomac run by Vikram Kothari, have swallowed thousands of crores of banking system and have run away. On the top of it they threat the Indian Banking system not to repay. Under such situation the Indian Banks have been pushed deeper into financial crisis.
- Public Sector banks remain capital restricted as bad loans have hit their capital ratios due to provision for NPA's and due to probability of default on account of loans.
- Another reason is the on-going problem since 2012 when banks started lending at a fast pace leading to a number of problem sectors such as telecommunication and mining.
- Loss of trust among the common people is another major problem. The rich are using the banks money in connivance while the middle and lower level have to bear the consequences of the misdeeds committed.

Record of Recapitalization In the Banking History :-

In the past 25 years the government has infused 3 lakh 60 thousand crores in the public sector banks in the name of recapitalization. Despite such massive investments, Life Insurance Corporation and Government of India which have high stakes in PSB's, they have not been able to put a required check on these banks.



According to the data by Bloomberg, in the year 1994, India had sold about 48 billion rupees of 12- year recapitalization bonds at a coupon rate of 10%. Despite using the taxpayers money to get these banks out of financial crisis earlier also, the Rs 2.11 lakh crores recapitalization is the largest till date.

The recapitalization amount is not small :-

The Government has proposed the recapitalization in the flowing manner:

- Budgetary allocations: Rs 18000 Crores
- Issue of equity shares by banks in the market: Rs 58000 crores
- Issue of Recapitalization bonds by the Government: Rs 1.35 lakh crores

The Government has proposed the above setup at the cost of public money collected in the form of taxes or from borrowing from various sources.

Banks continued to declare losses in 2018 :-

The mounting bad loans and bank losses has sparked the need to increase the Rs. 2.11 lakh crore recapitalization amount, for which the Government is already being questioned for its benefits if there are any. Many public sector banks are likely to continue reporting losses during FY18 caused due to elevated provisioning levels, decades of slipshod lending and lack of innovation and are likely to remain under PCA framework (Prompt Corrective Action).

As per an article in Nikkei Asian Review, which is an Asia-focused English-language publication having 140 years of quality journalism, the losses for the major banks in India are as follows:

- State Bank of India: Leading lender State Bank of India received 88 billion rupees in aid yet recorded a net loss of 77.18 billion rupees for the January-March quarter, down from a profit of 28.1 billion rupees in the year-ago period. Gross nonperforming loans totaled 2.23 trillion rupees, soaring from 1.78 trillion rupees in the comparable quarter last year.
- IDBI Bank: IDBI Bank, which received 106.1 billion rupees in aid, reported Friday a loss of 56.63 billion rupees in the quarter, wider than the net loss of 32 billion rupees in the year-ago period.
- Punjab National Bank: Punjab National Bank recorded the maximum loss of 134.17 billion as it made provisions to provide for the \$1.2 billion fraud. The bank received 54.73 billion as the aid for recapitalization.

How to win public trust :-

Due to the increasing concerns regarding the security of money and valuables, customers are losing faith in public sector banks. This is mainly due to increasing bank scams leading to difficulty for the small borrower in raising funds for start-ups. The way out is the introduction and implementation of stringent norms for to avoid re-occurrence of such large scale losses and NPAs. The banks should shift their focus to winning the trust of the depositors whose money is



being used for lending by banks, from writing off the debts. This will reduce the need for recapitalization and increase the profit margins.

Conclusion :-

It can be observed that recapitalization has definitely brought relief to the issue of NPAs and losses but for the continued growth and stability of public sector banks it is essential for these banks to focus on building customer trust by not lending indiscriminately and provide loans only in avenues where there is scope of recovery.

Your Turn

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