AIBEA's Banking News

5 & 6 MAY 2019

NEWS BULLETIN FROM ALL INDIA BANK EMPLOYEES' ASSOCIATION

'No guarantee that bank privatisation will be a panacea'

Raghuram Rajan
MAY 05, 2019
THE HINDU

'We need to recognise that ownership is just one contributor to governance, and look at pragmatic ways to improve governance across the board'

The banking system is overburdened with non-performing loans. Much of the problem lies in public sector banks, but private sector banks like ICICI and Axis Bank have not been immune.

Some of the malaise comes from a general need to improve governance, transparency and incentives in the system. However, the difficulties in even some private banks suggest that 'simple' solutions like privatising all public sector banks may be no panacea.

At any rate, banking reforms should tackle four broad areas: 1. Clean up banks by reviving projects that can be revived after restructuring debt. 2. Improve governance and management at public sector banks. 3. De-risk banking by encouraging risk transfers to non-banks and the market. 4. Reduce the number and weight of government mandates for public sector banks, and for banks more generally.

Privatise or not?

Is privatisation of public sector banks the answer? Much of the discussion on privatisation seems to make assumptions based on ideological positions.

Certainly, if public sector banks are freed from some of the constraints they operate under (such as paying above the private sector for low-skilled jobs and paying below the private sector for senior management positions, having to respond to government diktats on strategy or mandates, or operating under the threat of CVC/CBI scrutiny), they might perform far better. However, such freedom typically requires distance from the government. So long as they are majority-owned by the government, they may not get that distance.

At the same time, there is no guarantee that privatisation will be a panacea.

Some private banks have been poorly governed. Instead, we need to recognise that ownership is just one contributor to governance, and look at pragmatic ways to improve governance across the board.

There certainly is a case to experiment by privatising one or two mid-sized public sector banks and reducing the government stake below 50% for a couple of others, while working on governance reforms for the rest.

Rather than continuing a never-ending theoretical debate, we will then actually have some evidence to go on.

Some political compromises will be needed to allow the process to go through, but so long as the newly privatised banks are not totally hamstrung in their operational flexibility as a result of these compromises, this will be an experiment worth undertaking.

An alternative proposal to improve governance is to merge poorly managed banks with good banks. It is uncertain whether this will improve collective performance – after all, mergers are difficult in the best of situations because of differences in culture. When combined with differences in management capabilities, much will depend on whether the good bank's management is strong enough to impose its will without alienating the employees of the poorly managed bank.

We now have two experiments under way: State Bank has taken over its regional affiliates, and Bank of Baroda, Vijaya Bank and Dena Bank have been merged. The performance of the latter merger will be more informative. Thus far, market responses suggest scepticism that it will play out well. Time will tell.

De-risk banking by encouraging risk transfers to non-banks and the market

Too many risks devolve on to banks, including risks such as that of interest rate volatility that banks elsewhere typically lay off in markets. Too much project risk stays with banks because other financial instruments such as equity and subordinate debt cannot be issued cheaply.

Risk also returns through the back door.

For example, banks do not make loans to housing developers because of their intrinsic risks.

But they do make loans to non-bank financial companies, which make loans to developers. To prevent risk from returning to bank balance sheets, NBFCs must be able to raise money directly from markets.

Financial market development, addressed in Eswar Prasad's note in this volume, will help banks focus more on risks they can manage better and thus bear more effectively, while sharing or laying off what they cannot.

Banks will have to complement financial markets rather than see them as competition. The use of financial technology will be especially helpful to them in this endeavour.

Reduce the number and weight of government mandates for PSBs

Uncompensated government mandates have been imposed on public sector banks for a long time. This is lazy government – if an action is worth doing, it should be paid for out of budgetary resources.

Mandates also are against the interests of minority shareholders in public sector banks.

Finally, it does not draw the private sector in to compete for such activities. The government should incentivise all banks to take up activities it thinks desirable, not impose it on a few – especially as the privileges associated with a banking licence diminish.

Along these lines, requirements that banks mandatorily invest in government bonds (the SLR requirement) should continue to be reduced, substituting them instead with the liquidity coverage ratios and net stable funding ratios set by Basel. Among the more dangerous mandates are lending targets and compulsory loan waivers.

Government-imposed credit targets are often achieved by abandoning appropriate due diligence, creating the environment for future NPAs.

Loan waivers, as the RBI has repeatedly argued, vitiate the credit culture and stress the budgets of the waiving state or Central government. They are poorly targeted, and eventually reduce the flow of credit.

Agriculture needs serious attention, but not through loan waivers. An all-party agreement to this effect would be in the nation's interest.

Finally, the government should keep its banks well capitalised, conditional on improvements in governance and management efficiency. This is simply good accounting practice, for it prevents the government from building up contingent liabilities on bank balance sheets that a future government will have to pay for.

(Excerpted with permission from Juggernaut)

Rural pain goes beyond farmers, and it may be a problem for PM Modi

Reuters | May 3, 2019

THE FINANCIAL EXPRESS

The slowdown has also dented Prime Minister Narendra Modi's popularity in the hinterland that propelled him to power in 2014, and political strategists say it may mean he struggles to form a majority after voting in a staggered general election that began on April 11 concludes on May 19

Three years ago, brick mason Pundlik Bhandekar was always busy as farmers in his tiny hamlet in western India commissioned new houses and nearby towns were undergoing rapid urbanisation. Now, as the rural economy sinks and the pace of construction slows, Bhandekar is struggling to get work.

“I used to get a new construction project before I could even finish one. People would come to my house to check when I would be free to work for them,” said Bhandekar, as he sat with friends under the shade of a tree on a hot afternoon. From daily wage workers such as masons, to barbers and grocery shop owners – just about everyone in Zadshi village, some 720 km (450 miles) from India’s financial hub Mumbai, says a drop in farm incomes has dented their livelihoods.

Their woes are symptomatic of a wider problem across India, where more than half of the country’s 1.3 billion people are dependent on agriculture for their livelihoods, as the slowdown in the rural economy is felt in the dampening sales of consumer goods, especially the biggest such as car and motorbike sales.

The slowdown has also dented Prime Minister Narendra Modi's popularity in the hinterland that propelled him to power in 2014, and political strategists say it may mean he struggles to form a majority after voting in a staggered general election that began on April 11 concludes on May 19. Zadshi has been almost entirely dependent on annual cotton and soybean crops that, according to farmers, have given lacklustre returns in the past few years due to a dip in prices, droughts and pest attacks. And as incomes have dropped, farmers have cut back on big-ticket spending such as building new houses, digging wells or laying water pipelines, squeezing employment opportunities for people such as Bhandkekar.

"No one is interested in hiring us. We are ready to work even at 250 rupees ($3.60) per day," said Bhandekar, who charged 300 rupees a day when work was steady, but now gets work only once or twice in a fortnight.

LOWER WAGES, LESS SPENDING

Economic data reflects the plight of farmers and daily wage workers. Retail food inflation in the fiscal year ended on March 31 fell to 0.74 percent, even as core inflation stood at 5.2 percent, according to Bank of America Merrill Lynch Research, eroding the spending power of farmers. Inflation adjusted wage growth for workers involved in crop sowing was just 0.6 percent 2018/19 compared with 6.5 percent in 2013/14.

The value of farm produce at constant prices grew 15 percent in the past five years, compared with 23 percent in the previous five, while the manufacturing sector grew 40 percent, against 32.6 percent in the previous five years, government data shows.

"Lower rural wages will result in lesser spending, which in turn will reduce demand for goods and services that are part of the rural basket," Rupa Rege Nitsure, group chief economist at L&T Finance Holdings in Mumbai, told Reuters. The government needs to spend more in rural areas to generate employment and boost incomes, Nitsure said. Modi's Hindu nationalist government did introduce various support schemes in the past six months, such as a 6,000 rupees yearly handout to small farmers.

The main opposition Congress party has gone much further with its pledges though, saying it would introduce a basic minimum income, where the country's poorest families would get 72,000 rupees annually, benefiting some 250 million people.

RISING UNEMPLOYMENT

In Zadshi, as the mercury touched a searing 40C (104F), a group of villagers gathered under the trees lining a dusty road and began chatting about everything from crop prices to politics. "What else we can do? Had work been available in urban areas, we could have moved there but even in the cities construction has slowed down," said Amol Sontakke, an unskilled labourer who works in farms and on construction sites.

Job opportunities have slowed even in urban areas and India's unemployment rate touched 7.2 percent in February, the highest since September 2016, according to data compiled by the Centre for Monitoring Indian Economy (CMIE). Official data is unavailable for recent periods. The mood in Zadshi was glum. While four dozen villagers interviewed by Reuters were hopeful that if there was a good monsoon this year it could improve farm incomes, they've been cutting back on spending in the meantime.

"People are thinking twice before buying new clothes during festivals," said Avinash Gaurkar, a farmer currently doubling up as a part-time driver. "Buying big-ticket items such as motorcycles or refrigerators is out of the question."

Two years ago Gaurkar began building a house, but had to give up midway as his five-acre farm could not generate the money needed, he said, pointing towards a half-finished structure without doors. In 2018, just four villagers bought new motorbikes compared with as many as 10 a year about four years ago, said cotton farmer Raju Kohale, whose son is sitting at home unemployed after graduating as an engineer. "Poor monsoon or lower prices, something or the other has been hurting us in the past few years," Kohale said.

MODI AGAIN?

In the 2014 general election, most in Zadshi voted for Modi, but the farmers' distress has swayed many towards the opposition Congress party. That was clear from Reuters' interviews with 48 villagers, who cast their ballots last month. Farmers are at the bottom of the Modi administration's priority list, said labourer Sagar Bahalavi. "They are building big roads to connect metros and calling it development. How is that useful for us?" he said. Some, though, want to give Modi a second chance.

"Modi's intentions are good, it's the bureaucratic system that is not supporting him," said Gulab Chalakh, who owns a 20-acre farm and is among the richest in the village. "We should give him another chance."

Dangerous to let viable firms close down: Sahoo

PTI NEW DELHI, MAY 04, 2019 THE HINDU

'Law allows for errors to be corrected'

Committees of Creditors (CoCs) should provide all relevant information and share their vision for companies under the insolvency process, a senior official said on Saturday as he asserted that it would be dangerous to let viable firms to close down.

Amid rising number of stressed assets being referred for resolution under the Insolvency and Bankruptcy Code, the Insolvency and Bankruptcy Board of India chief M.S. Sahoo said the law also gave opportunities to rectify the mistakes during the insolvency process.

The objective of the law was to rescue viable companies and close down unviable ones, he said. "If due to incompetence [of market participants] the reverse happens, then it is dangerous," Mr. Sahoo said here.

"Commercial decisions are not black and white.

"There is no mathematical formula to say that a company is unviable and another is viable. It depends on so many considerations and who is looking at it."

NCLAT Chairperson Justice S.J. Mukhopadhaya said financial creditors should not play foul while going through the viability and commercial aspects of a resolution plan. Citing examples, he said operational creditors should also get money as do financial creditors in a resolution process.

Points of conflict

Prashanth Perumal J. MAY 05, 2019 THE HINDU

Why has the Supreme Court given an ultimatum to the Reserve Bank of India on loan defaulters?

The story so far: On April 26, the Supreme Court directed the Reserve Bank of India (RBI) to disclose to the public the names of willful defaulters on loans and also other information gathered by the central bank during its annual inspection of commercial banks. The RBI and the Supreme Court have been at loggerheads over this issue for a while now, with the central bank repeatedly refusing to obey the orders of the Supreme Court.

What did the RBI do?

In January 2016, the RBI refused to comply with demands made by activists under the Right to Information Act (RTI) to disclose copies of the annual inspection reports on banks such as the State Bank of India, Axis Bank, and ICICI Bank despite orders from the Supreme Court. The RBI also refused to provide information regarding the derivative losses suffered by banks and the fines imposed on banks by the RBI for violating various norms. The Supreme Court has this time around given the RBI a "last opportunity" to abide by its orders or face serious penal action. The disclosure of information about banks, however, is not the only point of conflict between two of the nation's powerful institutions. In early April, the Supreme Court quashed the RBI's circular issued on February 12, 2018 which directed banks to resolve their troubled loans within a period of 180 days. If banks failed to resolve their bad loans within the given deadline, the bad loan cases would be sent to bankruptcy courts.

Why does it matter?

The outcome of the battle between the RBI and the Supreme Court will determine the amount of information related to banks that will be made available to the public. Supporters of the Supreme Court's position believe that greater transparency will allow the general public and investors in public and private sector banks to make better decisions with their money. In particular, they point to the problem of willful defaults that has been plaguing banks. According to data gathered by TransUnion CIBIL, the amount of willful defaults has risen by four times in the last five years from Rs.39,504 crore at the end of March 2014 to Rs.1,61,213 crore at the end of December 2018. At the same time, the number of willful defaulters has doubled over the same period. State Bank of India, the largest public sector bank, has suffered the largest amount of willful defaults among all banks.

The disclosure of the names of willful defaulters to the public, many believe, will help bring about better credit discipline in the country by exposing problems brewing within banks sooner rather than later. In fact, they find it surprising that the RBI which has been spearheading the fight against bad loans is unwilling to release vital information on willful defaulters to the public. The RBI, on its part, has argued that the disclosure of auditing information related to banks can lead to the exposure of sensitive information that may not be in the commercial interest of banks or even in the interest of the wider economy. The RBI also seems to believe that releasing information about defaulters can unfairly shame borrowers who may genuinely not be able to pay back their loans due to various financial difficulties. Such shaming could have the unintended consequence of impeding genuine business activity in the economy. The central bank has also put forward the argument that it has the fiduciary duty to protect certain information about banks.

What lies ahead?

It is hard to predict what will happen next in this battle. The Supreme Court may begin contempt proceedings against the RBI if it chooses to disobey its latest order, but the impact this will have on the RBI's freedom remains to be seen. The RBI has chosen not to obey orders coming from the Supreme Court in the past, including previous proceedings of contempt against it. If the RBI is forced to abide by the Supreme Court order, it will certainly increase publicly available information on banks. Greater transparency will also help make the RBI more accountable. If there are legitimate reasons for banks and the RBI to withhold certain information from the public domain, however, the forced disclosure of information following the Supreme Court's order may lead to various unintended consequences both within the financial sector and the broader economy. The RBI, for instance, may choose to not include in its annual inspection reports certain sensitive information about banks that it feels shouldn't be in the public domain.

Saving BSNL

May 03, 2019 Editorial THE HINDU BusinessLine

The Centre needs to act urgently to revive this strategically important PSU

The Centre must take immediate steps to revive Bharat Sanchar Nigam Ltd if it wants to achieve the objective of reaching 100 per cent tele-density in rural areas and keep telecom services affordable for the common man. While private operators have taken over the market with billions of dollars in investments and cost-efficient operations, India's telecom consumers need a public sector entity like BSNL as an effective counter to any monopolistic venture that may arise due to the ongoing financial stress in the sector. From as many as nine operators, intense competition and below-cost pricing have reduced the number to just three players. The larger surviving operators, who have so far managed to sustain their operations, are under pressure to increase tariffs. The highly leveraged balance sheets of these operators could also force them to slow down the rollout of next-generation data networks to rural and economically unviable areas. In this context, it is important to have a strong PSU telecom company which will not only prevent private players from increasing tariffs as an easy means to escape financial stress but also ensure that rural consumers are catered to.

Reviving BSNL is tough, but not impossible. The once dominant public sector company has been reduced to a mere footnote, thanks to years of political interference and bureaucratic functioning. There have been many attempts earlier to improve the company's operations, but most of them remain on paper. For example, a committee headed by Sam Pitroda, then advisor to the Prime Minister, offered a 15-point plan to turnaround the PSU, including trimming staff, divesting 30 per cent equity, adopting a managed services model for its various operations and inducting a chief executive from the private sector. This plan has not been acted upon.

Time is running out, though. BSNL has, in 14 years, moved from Navratna status to being declared as a sick PSU, with cumulative FY2009-18 EBIT losses of Rs.82,000 crore. To prevent any further erosion of value, the Centre must do three things. First, divest all the real estate land parcels owned by the company and invest the proceeds into buying all the technology BSNL needs to be at par with private players. Second, implement the proposals of the Pitroda panel, especially those related to cutting down staff costs and hiving off various businesses into different verticals. Here, the Centre can study how British Telecom, once a struggling PSU in the UK, was turned around. Finally, remove all political interference and appoint a strong, independent management to run the company. This will not only secure the future of BSNL, but also ensure that affordable digital services reach every nook and corner of the country.

ALL INDIA BANK EMPLOYEES' ASSOCIATION
Central Office: PRABHAT NIVAS
Singapore Plaza, 164, Linghi Chetty Street, Chennai-600001
Phone: 2535 1522 Fax: 2535 8853, 4500 2191
e mail ~ chv.aibea@gmail.com
Web: www.aibea.in