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Recapitalisation and the Promise of Less Goverment

What is the issue?

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- Despite the costs to the exchequer, the decision to recapitalise banks have been largly well received.
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- The action has but added to the consistent shift away from the promise of ‘less government intervention’ for better governance.
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What is the price of Recapitalisation?

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- The government is to provide around Rs 1.5 lakh crore, over two years for recapitalising banks.
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- If the sum is assumed to be split evenly, the fiscal deficit this year will go up by about 0.4% of GDP.
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- This will come on top of the expected shortfall in non-tax revenues.
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- So that the year’s deficit could be about 4% of GDP - a slide from last year’s 3.5%, instead of moving forward to the targeted 3.2%.
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- It will also raise the ratio of government debt to GDP, which is already too high.
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Is government intervention increasing?

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- **Banking -** More than 70% of the fresh capital to be pumped in is to come from the government.
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- Notably, in many banks the extent of government shareholding has slipped to well below that level.
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- This means recapitalisation in the manner announced will raise the level of government ownership in banks.
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- This would be a policy reversal from the early 2000s (Narashiman Committee Recommendations), that intended to reduce government's stakes in banks.
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- **Forced Bailouts -** The public shares issued by General Insurance Corporation (a PSU) got a poor response.
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- Among institutional investors, the biggest investors were other government owned entities like the Life Insurance Corporation.
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- As the list also featured some government banks there is suspicion that government had proded them to bail out the shares issued.
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- Notably, since the price of the new shares fell immediately on listing, all investors have lost value at the moment.
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- **Trend -** Increased government role has been felt in pharmaceuticals through price controls.
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- Vigourous pursuit of Aadhaar related compliance is seen as an intrusive approach by an over-zealous government.
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- Hence, increased government interventions has been felt across sectors and is indicative of a trend rather than isolated incidences.
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- **Private Withdrawal -** Meanwhile, the private sector's role in infrastructure creation has become more cautious.
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- Even new sectors that opened to the private, like 'defence production' has made little progress.
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What is the way ahead?

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- The current regime is clearly faultering on its promise of reducing government's interventionist approach.
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- But the opposition too doesn't offer much solace in this regard and has rather vouched for a more interventionist leftist agenda.
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- The pressure of slowing growth and lack of jobs has been driving most of the present internventions.
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- It is to be noted that enhanced GDP growth is what would provide more head room for both pro-market policies and increased welfare speanding.
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Source: Business Standard

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