



# IAS PARLIAMENT

*Information is Empowering*  
A Shankar IAS Academy Initiative

## Recapitalising PSBs

### What is the issue?

- Finance Minister said that the Centre will not infuse any further equity into public sector banks (PSBs).
- So, the market-based fund-raising and higher retail ownership is the way forward.

### Why this decision is welcomed?

- This is welcome given that Covid-related business disruptions are widely expected to escalate capital requirements for PSBs.
- Their actual capital needs will depend on many moving parts.
- Estimates suggest that PSBs may require new capital between ₹35,000 crore and ₹85,000 crore in the second half of this fiscal, to maintain their capital buffers.
- Funding this will certainly stretch the fisc at a time when the priority is resuscitating the economy.
- But weaning PSBs away from their government dependence is desirable for other reasons as well.

### What happened in the past?

- In the last three years, the Centre has already infused ₹3.5-lakh crore into PSBs with very little to show for it.
- Each round of capital infusion is made with the intent of improving credit flow to the economy.
- But, in practice, the bulk of capital tends to be absorbed by bad loan provisions, while bankers continue to display endemic risk aversion.
- Attempts to make these infusions selective and contingent on individual PSBs' performance have not worked either.
- This is because the tottering banks need to be shored up before eroding depositor confidence can pose systemic risks.
- This situation results in a moral hazard where the government is forced to commit ample taxpayer money towards PSB recapitalisation every year with

very little payback.

### **What is the challenge?**

- There can be no doubt that the government cutting its apron strings in PSBs is the best way forward.
- But, getting public shareholders to subscribe to these offers will be no mean task.
- There were sluggish credit growth and loan losses in the recent past.
- Due to this, even leading PSBs have poor profitability and return ratios that compare unfavourably to private sector peers, with their stock prices languishing well below book value.

### **What could help?**

- Infusing fresh capital at these bargain-basement valuations, apart from diluting earnings for existing investors can actively deter new ones.
- Kicking off long-pending governance reforms can partly solve this problem.
- It will shore up market valuations and investor sentiment towards PSBs.

### **What are the suggestions?**

- The PJ Nayak committee suggested a few of the reform measures.
- It suggested creating an umbrella holding company to house government stakes in all PSBs.
- It also suggested distancing the government from commercial decisions by appointing independent boards and CEOs.
- Other suggestions include extending top management tenure and ushering in performance-linked pay at PSBs.

**Source: Business Line**



**IAS PARLIAMENT**  
*Information is Empowering*  
A Shankar IAS Academy Initiative