AIBEA's Banking News

5,6,7 FEBRUARY, 2021

NEWS BULLETIN FROM ALL INDIA BANK EMPLOYEES' ASSOCIATION

Public Banks Q3'21 Results

Net Profit (In Crores)

SBI - 5,196

BOB- 1,159

Canra- 750

UBI - 727

Indian- 514

PNB - 506

BOM - 154

UCO - 35

Awaited BOI, CBI, IOB, P&Sind

Can a 'bad bank' solve the growing NPA crisis?

Prashanth Perumal J. FEBRUARY 07, 2021 THE HINDU

What is the Budget proposal on non-performing assets, and can it help recapitalise public sector banks?

The story so far: Finance Minister Nirmala Sitharaman in her Budget speech on Monday revived the idea of a 'bad bank' by stating that the Centre proposes to set up an asset reconstruction company to acquire bad loans from banks. While the problem of bad loans has been a perennial one in the Indian banking sector, the COVID-19 pandemic-triggered lockdown last year and the moratorium subsequently extended to borrowers by the Reserve Bank of India (RBI) have worsened the crisis. With banks expected to report even more bad loans this year, the idea of a 'bad bank' has gained particular significance.

What is a 'bad bank'?

A bad bank is a financial entity set up to buy non-performing assets (NPAs), or bad loans, from banks. The aim of setting up a bad bank is to help ease the burden on banks by taking bad loans off their balance sheets and get them to lend again to customers without constraints. After the purchase of a bad loan from a bank, the bad bank may later try to restructure and sell the NPA to investors who might be interested in purchasing it.

A bad bank makes a profit in its operations if it manages to sell the loan at a price higher than what it paid to acquire the loan from a commercial bank. However, generating profits is usually not the primary purpose of a bad bank — the objective is to ease the burden on banks, holding a large pile of stressed assets, and to get them to lend more actively.

What is the extent of the crisis faced by banks?

According to the latest figures released by the RBI, the total size of bad loans in the balance sheets of Indian banks at a gross level was just around ₹9 lakh crore as of March 31, 2020, down significantly from over ₹10 lakh crore two years ago.

While the size of total bad loans held by banks has decreased over the last few years, analysts point out that it is mostly the result of larger write-offs rather than due to improved recovery of bad loans or a slowdown in the accumulation of fresh bad loans.

The size of bad loan write-offs by banks has steadily increased since the RBI launched its asset quality review procedure in 2015, from around ₹70,000 crore in 2015-16 to nearly ₹2.4 lakh crore in 2019-20, while the size of fresh bad loans accumulated by banks increased last year to over ₹2 lakh crore from about ₹1.3 lakh crore in the previous year. So, the Indian banking sector's woes seem to be far from over.

Further, due to the lockdown imposed last year, the proportion of banks' gross non-performing assets is expected to rise sharply from 7.5% of gross advances in September 2020 to at least 13.5% of gross advances in September 2021.

What are the pros and cons of setting up a bad bank?

A supposed advantage in setting up a bad bank, it is argued, is that it can help consolidate all bad loans of banks under a single exclusive entity. The idea of a bad bank has been tried out in countries such as the United States, Germany, Japan and others in the past.

The **troubled asset relief program, also known as TARP**, implemented by the U.S. Treasury in the aftermath of the 2008 financial crisis, was modelled around the idea of a bad bank. Under the program, the U.S. Treasury bought troubled assets, such as mortgage-backed securities, from U.S. banks at the peak of the crisis, and later resold them when market conditions improved. According to reports, it is estimated that the Treasury through its operations earned nominal profits.

Many critics, however, have pointed to several problems with the idea of a bad bank to deal with bad loans. Former RBI governor Raghuram Rajan has been one of the critics, arguing that a bad bank backed by the government will merely shift bad assets from the hands of public sector banks, which are owned by the government, to the hands of a bad bank, which is again owned by the government. There is little reason to believe that a mere transfer of assets from one pocket of the government to another will lead to a successful resolution of these bad debts, when the set of incentives facing these entities is essentially the same.

Other analysts believe that unlike a bad bank set up by the private sector, a bad bank backed by the government is likely to pay too much for stressed assets. While this may be good news for public sector banks, which have been reluctant to incur losses by selling off their bad loans at cheap prices, it is bad news for taxpayers, who will once again have to foot the bill for bailing out troubled banks.

Will a 'bad bank' help ease the bad loan crisis?

A key reason behind the bad loan crisis in public sector banks, some critics point out, is the nature of their ownership. Unlike private banks, which are owned by individuals who have strong financial incentives to manage them well, public sector banks are managed by bureaucrats who may often not have the same commitment to ensuring these lenders' profitability. To that extent, bailing out banks through a bad bank does not really address the root problem of the bad loan crisis.

Further, there is a huge risk of moral hazard. Commercial banks that are bailed out by a bad bank are likely to have little reason to mend their ways. After all, the safety net provided by a bad bank gives these banks more reason to lend recklessly, and thus, further exacerbate the bad loan crisis.

Will it help revive credit flow in the economy?

Some experts believe that by taking bad loans off the books of troubled banks, a bad bank can help free capital of over ₹5 lakh crore that is locked in by banks as provisions against these bad loans. This, they say, will give banks the freedom to use the freed-up capital to extend more loans to their customers. This gives the impression that banks have unused funds lying in their balance sheets that they could use if only they could get rid of their bad loans. It is, however, important not to mistake banks' reserve requirements for their capital position. This is because what may be stopping banks from lending more aggressively may not be the lack of sufficient reserves, which banks need to maintain against their loans.

Instead, it may simply be the precarious capital position that many public sector banks find themselves in at the moment. In fact, many public sector banks may be considered to be technically insolvent as an accurate recognition of the true scale of their bad loans would show their liabilities as far exceeding their assets. So, a bad bank, in reality, could help improve bank lending not by shoring up bank reserves, but by improving banks' capital buffers.

To the extent that a new bad bank set up by the government can improve banks' capital buffers by freeing up capital, it could help banks feel more confident to start lending again.

Public sector banks in turmoil after mega merger: Parliament panel

Flags their low market valuations, says it'll hinder plans to raise equity

Nikunj Ohri | New Delhi February 3, 2021 **BUSINESS STANDARD**

The mega merger of public sector banks (PSBs) has led to a “turmoil” as the state-owned banks do not have the necessary talent for specialised functions like risk management and new financial technologies, the Parliamentary Standing Committee on Finance said in its report.

“PSBs are also going through considerable turmoil because of the mega mergers; this will require even closer assessment of human resources to ensure that sufficient management talent is available for the PSBs as they seek to streamline and expand their operations,” according to the report of the committee, chaired by BJP MP Jayant Sinha.

From April 1, 2020, ten PSBs were amalgamated into four, taking the total number to 12.

After the merger exercise, Punjab National Bank, Oriental Bank of Commerce, and United Bank of India combined to form one lender; Canara Bank took over Syndicate Bank; while Union Bank of India amalgamated with Andhra Bank and Corporation Bank. Indian Bank subsumed Allahabad Bank.

With the new privatisation policy announced in the Budget, the government has announced that four broad sectors, including banks, will have “bare minimum” government presence with the remaining being privatised, merged or subsidiarised with other CPSEs.

The panel also said the government should fully clarify the functioning of the Banks Board Bureau (BBB), and the BBB should assist PSBs in acquiring and retaining such specialised talent.

Strengthen PSB competitiveness

The parliamentary panel also raised concerns on the “depressed” market valuations of state banks.

“PSBs continue to have very low price-book multiples and their market valuations remain depressed. The committee notes that the PSBs do not appear to have differentiated strategies that will enable them to compete effectively," said the report.

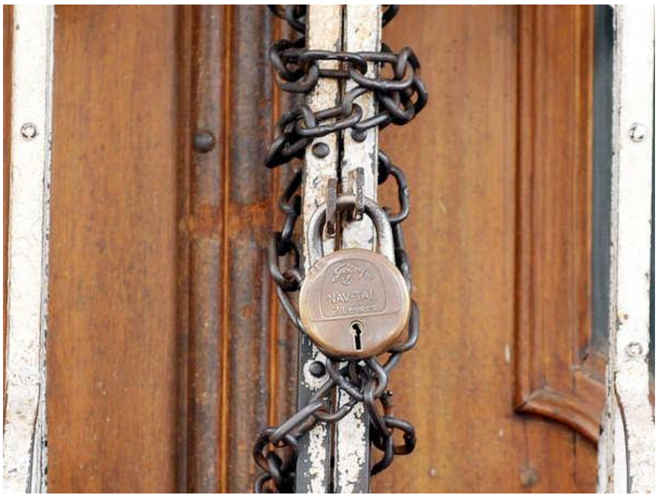
Apart from the mega mergers, the Department of Financial Services should also prepare a comprehensive plan on how to strengthen PSB competitiveness, the report said. Low valuations imply that banks will find it difficult to raise equity through the markets, it said.

As a result, if NPAs increase yet again due to adverse global trends, significant funding will be required from the government to keep PSBs appropriately capitalised.

On this observation, the government replied that it has adopted a measures to reform PSBs, and strengthen their competitiveness, which include industry-linked improvement in turnaround time, digital banking services, competitive pricing, customer-need driven marketing strategy and reach, prudential lending and effective loan life-cycle management

Bank unions strongly oppose divestment, a bad bank and threaten to strike

PRABHJOTE GILL FEB 3, 2021, ***BUSINESS INSIDER***



Banks are threatening to go on strike if the government moves forward with its plan to disinvest public sector banks and Life Insurance Corporation

- **The All India Bank Officers' Confederation (AIBOC) and the All India Bank Employees Association (AIBEA) are not on board with the Indian government's plans to disinvest stake in banks.**
- **According to them, selling government stake in public sector banks and Life Insurance Corporate (LIC) would threaten the stability of the sector.**

- **Both organisations are threatening to strike if the government moves forward with its plans as announced by Finance Minister Nirmala Sitharaman during the Budget 2021-22 on February 1.**

Banking unions aren't happy with the government's plans to divest stake in public sector banks (PSBs). The All India Bank Officers' Confederation (AIBOC) released a harshly worded statement opposing the announcements by Finance Minister Nirmala Sitharaman during the Budget 2021-22.

"Four officers' organisations representing the entire fraternity of officers in the banking industry deeply deplore and resolutely oppose the proposal of the Honorable Finance Minister Nirmala Sitharman in Union Budget 2021, which propose the privatisation of two public sector banks and one general insurance company," read the statement.

The All India Banks Employees Association (AIBEA) — the largest trade union of bank employees which consists of officers as well as clerical staff — is also against PSB privatisation.

"Privatising them means handing over the people's money to private hands with vested interest," it said in its own statement, warning of possible strikes.

The United Forum of Bank Unions (UFBU) — an umbrella body of nine unions including the AIBEA and AIBOC — has proposed going on strike on February 4, either during lunch hours or after office hours. However, past attempts and strikes to halt the privatisation of public sector banks have been unsuccessful.

Employees of Allahabad Bank demonstrate during an all India bank strike called by United Forum of Bank Unions in Patna in 2017 against privatisation of government banks and demanding implementation of Parliamentary Committee

Bad banks and more FDI in insurance is a bad idea say unions

The AIBEA is also against the idea of a bad bank or Asset Reconstruction Company (ARC) to house non-performing assets (NPAs). According to them, the idea will only remove corporate defaults from the books, not fix the underlying issue. A number of experts too believe that a bad bank could create a moral hazard.

Furthermore, the unions are displeased with the government decision to increasing the cap of foreign direct investment (FDI) in the insurance sector from 49% to 74%. This will give foreign companies controlling stake in insurance companies.

Members of United Forum of Bank Unions staging a protest opposing privatisation of public sector banks at State Bank of India in Bangalore in 2008

Where is the government selling stake?

The aforementioned 'general insurance company' refers to the Life Insurance Corporation of India (LIC). While the names of two public sector banks have not been specified, analysts believe the most likely candidates are Bank of Baroda (BoB) and Punjab National Bank (PNB).

Both these banks have seen their balance sheets extended with the merging of smaller public sector banks. BoB absorbed Vijaya Bank and Dena Bank. PNB took on United Bank of India and the Oriental Bank of Commerce. In July last year, NITI Aayog recommended the privatisation of UCO Bank, Punjab & Sind Bank and Bank of Maharashtra.

Employees stage a protest in support of the two-day nationwide strike against the Privatisation of IDBI Bank and demanded that stringent measures should be taken to recover the Bad Loans on 10 August 2018

'Disinvestment poses a threat to the dominance of PSBs'

The unions believe that disinvestment proposals will weaken India's self-reliance and make them dependent on foreign capital and the private sector.

India now has 12 PSBs, down from 27 in 2017. They collectively contribute to around 60% of banking in the market.

Balance sheet	Percentage of ownership by public sector banks
Deposits	64%
Loans and advances	60%

Unions believe that more private players in the sector could lead to instability. "The dominance of public sector banks insulated the Indian economy from the consequences of the 2008-09 financial crisis," the unions' justify.

'Government needs public sector banks to implement its policies'

AIBOC also asserts that government schemes like the Jan Dhan Yojana and MUDRA have been successful because of PSBs and their rigorous implementation.

During the pandemic, the unions say that PSBs were instrumental in implementing measures to provide liquidity and fiscal stimulus. "We consider any proposal for privatisation of public sector banks is retrograde, ill-conceived and thoroughly inimical to the national interest," said the statement.

But, what about the rapidly increasing bad loans? PSBs have often been criticised for accumulating bad-debt dues to big-ticket corporate defaults. This leads to massive haircuts through the debt-recovery channel.

AIBOC explains that despite that being true, PSBs have been able to register positive operating profit.

"In this backdrop and at a time when the national economy is still reeling under the impact of a severe recession caused by the COVID-19 pandemic, we cannot fathom why the Union gGovernment is keen on the privatisation for public sector undertakings in general, and PSBs in particular," it said.

The unions also say that the divestment plans will only serve the interests of corporates with a lot of debt.

"Any step towards privatisation, dilution of government equity or further mergers and amalgamation of public sectors would face stiff resistance, not only from our organisation but also from all the major stakeholders," warned AIBOC asking the government to retract its proposal.

"The Union Government should rather initiate policy discussion on the ways and means of reforming and strengthening the public sector banks," it proposed.