GS-III: Making the grand India PSB mergers work.

News

The initial enthusiasm of market analysts to the bank merger announcement is giving way to wariness and scepticism.

Procedure of Bank Merger

- An application for merger is submitted by the concerned banks to the Central Registrar of Cooperative Societies (CRCS).
- A copy of the application is also sent to Reserve Bank of India (RBI) along with valuation report and information relevant for consideration of the scheme of merger.
- The RBI then examines the scheme in respect to the interests of depositors and conveys its decision to the CRCS.

What is the rationale behind the mergers?

- It was the Narasimham Committee in the late 1990s that recommended consolidation through a process of merging strong banks.
- There are too many banks in India with sizes that are minuscule by global standards with their growth constricted by their inability to expand.
- Given this, the biggest plus of the mergers is that they will create banks of scale.
- According to the government, banks have been merged on the basis of likely operating efficiencies, better usage of equity and their technological platform.
- But the move marks a departure from the plan to privatise some of the banks or bringing in strategic investors to usher in reform in the sector.
- The government has decided amalgamation as the “best route” to achieve banking sector scale.
- This is also expected to support the target of achieving a $5 trillion economic size for India in 5 years.
- However, mergers may not lead to any immediate improvement in their credit metrics.

How effective could the merger be?

- Bank consolidation is a good move towards improving efficiency of the PSBs.
- This would enable the consolidated entities to meaningfully improve scale of operations and help their competitive position.
- Given that the merged banks are on similar technology platform, the integration should be smoother.
- However, there may not be any immediate improvement in their credit metrics as all of them have relatively weak solvency profiles.

What are the challenges and priorities now?

- Mergers are driven by synergies in products, business, geographies or technology and the most important, cost synergies.
- There may be some geographical synergies between the banks being merged now.
- But unless banks realise cost synergies through branch and staff rationalisation, the
mergers may not mean much to them or to the economy.
- This is where the government’s strategy becomes significant.
- Evidently, public sector banks are overstaffed.
- But the **key reforms to be made are at the board level**, including in appointments, especially of government nominees.
- These are often political appointees, with little exposure to banking.

**Way forward:**

While such consolidation can result in handsome productivity gains, what matters is the quality of execution by at stable and committed leadership aided by a shrewd and benign ownership.