# Governance Issues - Public sector banks

## Why in news?

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Bad loans of public sector banks are Snowballing and it poses a systemic risk to the country's economic system.

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## What are the issues plaguing the PSB's?

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- Banks lend longer term loans to large infrastructure projects, although their expertise lies in granting short term working capital loans.
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- Senior government officials, with political backing, hold overarching control over banks.
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- This has led to poor choice of the top management for the banks and inadequate governance standards.
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- RBI's latest **financial stability report** considers the risks of asset quality deterioration and additional capital requirement of banks to be "high".
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- This was shown by huge write-offs on PSB's loans, once the firms go in for bankruptcy and the subsequent necessity for huge recapitalisation of the banks.
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- Though it creates a substantial fiscal burden, it is necessary to enable the banks meet their minimum **capital adequacy requirements**.
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- Even then banks will generate a substantial pile of fresh bad debts, if there is no change in the governance structures that created bad loans before.
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### What are the measures taken so far?

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- Banks Board Bureau was created to bring about a fundamental change in the selection of top management and governance standards.
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- Asset quality reviews was initiated in order to end window-dressing and recognise non-performing assets (NPAs) to **avoid evergreen lending**.
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- Large NPAs of over Rs.2,000 crores, once failed to achieve a resolution within 180 days will have to be referred immediately under IBC.
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### How Project sashakt will be useful in this regard?

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- Large defaulters, above Rs.500 crores, will be brought under it to create a vibrant market for **online trading of stressed assets**.
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- Banks will first pass on the defaulted accounts to an asset reconstruction company(ARC).
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- ARC will restructure the assets, define haircuts and transfer their ownership to one or more asset management companies (AMCs), which will be funded by sector-specific alternative investment funds (AIFs).
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- This makes banks to get paid for the restructured assets with the ownership passing on to the AMC-AIFs.
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- Failure to complete the process in 180 days will attract IBC proceedings under NCLT for the stressed company.
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- Still it doesn't make much headway, since bank managements become reluctant to agree to substantial haircuts or discounting of their dues.
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### What is the way forward?

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- Around 60% of experts feel that “continuous rise of NPAs and falling governance standards in banks continue to be a cause for concern.”
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- The RBI says in its **annual report for 2017-18** that over the medium term growth will depend on “resolution of banking and corporate financial stress.”
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- **Both IBC and Sashakt take care of “continues rise in NPAs” but not “governance standards”**.
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- Hence, bad debts will reappear with the government being compelled to recapitalise the banks again.
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- That would amount to a systemic risk with fiscal instability and insufficient bank credit becoming a periodic feature in the country.
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**Source: Business Line**

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