

Business Standard

Govt to soon bring corporate governance norms at state-owned banks

Improving the quality of credit appraisal at these banks is among the likely changes

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The government is planning to refresh the corporate governance norms for state-owned banks. The changed rules could be announced even before the Union Budget is presented, it is learnt.

Improving the quality of credit appraisal at these banks is among the likely changes. The governance reforms, as an official put it, would bring in measures to track the performance of the executive-rank employees of the banks, intensively. The proposed steps would also respond to Moody's criticism that reforms needed for efficiency and better operating performance were absent at public sector banks. Without such reforms, "the sector would continue to represent a contingent liability to the sovereign", the second largest rating agency in the world had said last November.

"From now instead of a hands-off approach, we intend to be hands-on," said another officer, aware of the developments. According to him, other than wilful negligence, neglect of human resources had brought the state-run banks to their present state, especially in credit appraisal.

In an earlier report, a Reserve Bank of India committee had recommended additional qualifications for bank staff to be posted in credit operations, treasury and risk management areas. It is yet to be implemented.

The move is being seen as a balance between an outright privatisation of banks, which is considered politically unfeasible, and the option to let them continue with a business-as-usual approach. In the current financial year, the finance ministry had to step in with a bailout package of Rs 2.11 trillion, to be paid over the next few years to the ailing public sector banks (PSBs).

While the bailout has assuaged large investors about the immediate financial solvency of banks, there are doubts among them about how far the money would shore up the balance sheets of banks unless the quality of lending improves. The changes could also decide which way the Bank Boards Bureau would move. The Bureau headed by former CAG Vinod Rai was supposed to be entrusted with such a role but a turf war between the Department of Financial Services and the Bureau came in the way.

The government's Indradhanush plan, the first phase of the bailout package, had also hinted that the Bureau would be tasked with helping these banks make necessary changes in their corporate governance models.

The government believes that since the operational performance of banks means so much to the rating agencies, it makes sense to bring in wide ranging changes in the operations of banks. As a joint study by IIM Calcutta, Indian Institute of Corporate Affairs and Thought Arbitrage Research Institute showed, there is a strong correlation between standards of corporate governance in banks and the performance of their share prices.

The finance ministry expects to drive the changes in its capacity as the largest shareholder in these banks. It is also holding negotiations with bank employees for wage revision, making it the right time to drive the changes.

The official said mere consolidation among the banks would not help unless the incentive structure was reorganised among the bank employees to make credit appraisal their key competency.

A paper written by Eswar Prasad and Isha Agarwal for Brookings India recently made the same point. "Reforms are needed to make PSBs more accountable and change their incentive structures such that their lending practices are in line with the productive allocation of credit. This can be achieved by adopting better governance practices and providing more autonomy to PSBs."