

# Do we really need PSU banks? Not at all – Here is why

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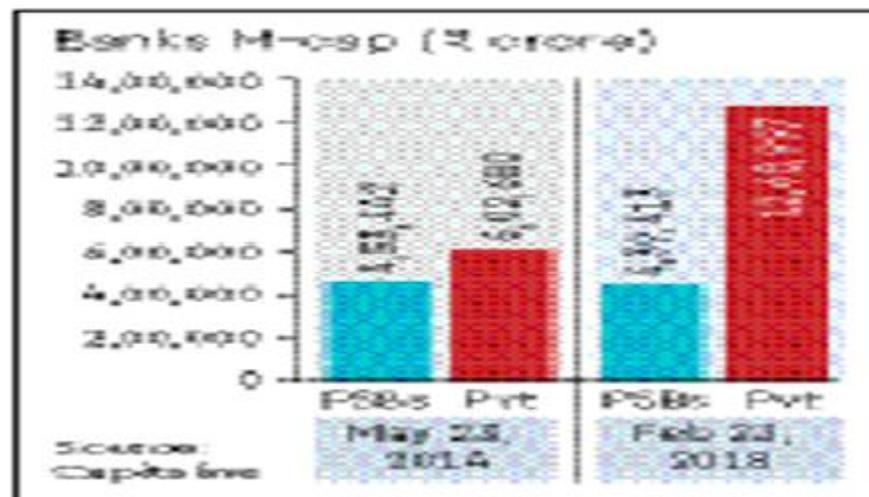
After Rs 58,000 crore was infused into public sector banks under the Indradhanush plan since FY16—and another Rs 66,624 crore from FY11 to FY15—it is not just the government, but the Opposition parties that need to seriously ask whether India needs public sector banks. (Reuters)

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After Rs 58,000 crore was infused into public sector banks under the Indradhanush plan since FY16—and another Rs 66,624 crore from FY11 to FY15—it is not just the government, but the Opposition parties that need to seriously ask whether India

needs public sector banks. More so since, over the next two years, the government plans to pump in another Rs 211,000 crore into these very banks. The money, pumped in by the UPA and then the NDA governments, has been given to recapitalise the banks, that is, to make good the losses they have made by giving loans to industry that have turned into NPAs. It is no one's case that only loans given by PSU banks have turned into NPAs since private sector banks also have large NPAs. Nor is it true that all these NPAs are due to siphoning off of funds by the likes of Nirav Modi. Yet, it remains true that PSU banks tend to have a higher proportion of NPAs, partly because they lent more to industry than the private sector banks did. But the government cannot afford to spend Rs 300,000-350,000 crore every decade on PSU banks. Nor is this the only value destruction. When prime minister [Narendra Modi](#) came to power, PSU banks had a market capitalisation of Rs 453,442 crore or around 43% that of the entire banking sector (see graphic). By February 23 this year, the PSU banks had lost a bit of this value and had a market capitalisation of Rs 439,413 crore.

Private sector banks, however, saw their market capitalisation zoom from Rs 602,680 crore to Rs 1,268,997 crore over the same period, as a result of which the share of PSU banks in total bank market capitalisation fell from 42.9% to just 25.7%. Compared to a situation where PSU banks retained their market-capitalisation share, this means a notional loss of Rs 280,000 crore! And this is despite the government pumping in Rs 124,000 crore already since FY11 and planning another Rs 210,000 crore over the next two years. That, by most standards, is colossal value destruction, and we have not even seen the changes that are going to happen thanks to the fintech and payments revolutions. The same argument of value-destruction probably applies to all PSUs, not just banks, but after the latest round of funds-infusion and the PNB scam, it is PSU banks that are in focus. In the period since Modi came to power, the share of PSU banks in total deposits is down from 79.8% to 75.7%, but the share in loans—which is where banks make the bulk of their money from—is down from just 78.8% to 70.8%. If PSU banks have not lost more of the share of bank deposits, it is because people feel their money is safe in PSU banks, but an eight percentage point fall in advances over 40 months is a lot.



Chances are most politicians will argue that while the value destruction is large, the benefits for the poor—via the PSU banks—are a lot more important. So, whether it is politicians in the [Congress](#) or the [BJP](#), whether it is [Rahul Gandhi](#) or Narendra Modi, all will talk of the lakhs of crore that banks lend to agriculture—the latest budget, in fact, has raised the target for bank lending to this sector from Rs 10 lakh crore in FY18 to Rs 11 lakh crore in FY19. They will also talk of how, since Modi has come to power—Rahul Gandhi will cite similar data for when Dr Manmohan Singh was prime minister—it was mainly public sector banks that opened Jan Dhan accounts, they will talk of the hugely subsidised loans that are being given for housing for the poor...

Much of this is true, but it is missing the woods for the trees. Lending to agriculture or MSMEs is mandated by [RBI](#), as a share of total lending; so if, for the sake of argument, all PSU banks are privatised, private banks will have to do this much of lending. Private banks, it is true, will not open Jan Dhan accounts like the PSU banks did, but if the government paid them to do so, and to service these loans, they would gladly do this. That's where the massive value erosion by PSU banks and the capital being pumped in come in—the government would have to spend a fraction of this to get the Jan Dhan accounts set up and serviced. Ditto for the housing subsidies—in any case, the government pays even PSU banks for these. The short point is that if there is any service PSU banks did for the poor, the government can transfer the cost of this directly to their bank accounts using DBT and they can afford to pay the charges of private banks.