

## Confidence in working of PSBs at a historically low level: YV Reddy

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File Photo of Y V Reddy, former RBI Governor. - BusinessLine

“Banks benefit from fiscal stimulus, monetary stimulus and regulatory forbearance”

**MUMBAI, JUN 10**

The doubts about trust in banks that have arisen in recent months could be attributed, among others, to mounting non-performing assets on account of defaults by the very rich; a proposal to resolving the issues of problem banks by making depositors share the burden of insolvency; large criminal frauds committed in select banks; and the investigations launched and raided members and CEOs, according YV Reddy, former Reserve Bank of India Governor.



Referring to several policy actions taken by Government and RBI in response to the global financial crisis, Reddy observed that the banks benefitted from fiscal stimulus, monetary stimulus including higher exposure limits to corporates, groups and industries.



“In retrospect, perhaps, the extra-ordinary measures taken were more than needed and, were continued for longer period than necessary. Banks had also been encouraged to lend to infrastructure, which was not the core competence of the banks, apart from creating asset and liability mismatch.

“Disclosures of real position were delayed. So, the accumulated problems came to the open in 2013-14 and in subsequent years,” said Reddy, who was the RBI Governor from September 6, 2003 to September 5, 2008. He was also Deputy Governor at the central bank from 1996 to 2002.

This affects the depositors if a bank does not have enough money to pay the depositors, that is, when the capital is not adequate, he said in his speech on ‘Keeping Banks Safe’ at Shivaji University, Kolhapur last evening.

Reddy, however, emphasised that bank deposits continue to be as safe as they have ever been, as far as private sector banks are concerned. They have adequate capital. “The public sector banks do not have adequate capital to take care of the depositors interest, but since the majority ownership is that of the government, the deposits are safe. These are not limited liability companies, but institutions established under the law. However, the depositors are protected with the tax-payers money.

“People know this instinctively and, therefore, do not rush to withdraw deposits. The uncertainty and delay in Government’s injecting of capital as required by the RBI is a source of discomfort, no doubt. In any case, the tax payer has to pay for high NPAs since Government as owner has to bear the burden,” he explained.

## PSBs: confidence at a historic low

In this regard, the former RBI Governor observed that “the confidence in the working of the public sector banks is at a historically low level. The future of the public sector banking which accounts for a major part of the banking system is uncertain. They are functioning without knowing where they would be.”

The former RBI Chief opined that there should be clarity on the future of public sector banking towards which the government should move. The objective for public ownership of banks should be clarified and simplistic comparisons with the private sector banks avoided.

## Bail-in proposal

Referring to the 2017 proposal to amend the law relating to resolution of banks and financial institutions, Reddy said the objective was to equate the bank depositor on par with other creditors.

He opined, “this caused nationwide concern, and rightly so. Fortunately, the law has been deferred or dropped. In any case, private sector banks are adequately capitalised and, therefore, there is no issue now. Yet the (bail-in) proposal has itself created a panic, and some withdrawal of deposits took place. To an extent, some permanent damage has been done to the trust in safety of bank deposits.”

## Bank Frauds: Owner should be worried

Referring to the PNB scam, the former RBI Chief said it is clear that it is a fraud. The focus of all institutions should be to punish those who indulged in fraud and benefited most from the fraud. It is a crime and investigation of the crime should be the top most priority.

“Who should be worried most about the fraud? The owner of the bank who stands to lose most. The owner is the Government. The owner should be worried about what the Directors it nominated in the Board, were doing. The owner should be worried about the Managers it appointed. The owner should be worried about the system of monitoring and control of its own investment. That should be the focus of the owner,” he added.

Underscoring that tax payers end paying for the losses due to the fraud, Reddy felt that the tax payers who have entrusted their money to the Government owned banks should be asking the government to explain why as the custodian of their money it failed to prevent the fraud.

## Is RBI responsible?

Though its main responsibility is financial system stability and the depositors protection, the central bank cannot escape responsibility for maintaining the trust of the public in the banking system, emphasised Reddy. “The fraud is of such a magnitude that it affects the credibility of RBI in ensuring the trust of people in banking. To this extent, it has to review its own regulatory and supervisory practices,” he said.

Despite criticisms in some segments of media, Reddy felt that RBI is held high in peoples esteem. However, he underscored that actions taken by Government and official statements should ideally reinforce confidence in the RBI at this juncture.

RBI should be seen to command respect and backing of Government to continue to effect mergers to protect depositors interest...effectiveness of RBI will be enhanced with demonstrable support from the Government,he added.

# Raids and Investigations

Terming the recent large scale operations undertaken by the Central Bureau of Investigation (CBI) as unprecedented, Reddy observed that most of them are based on conspiracy and implied loss to Government than bad motive or pecuniary gains.

“Raids and investigations may be intended to (a) punish the guilty, and (b) act as a deterrent. Whether the really guilty have been booked; whether they will be punished finally; and whether they act as a deterrent are questions that remain.

“But, what is certain is that there is loss of confidence in the integrity of the banking system. It is not clear whether this by itself enhances the trust and whether there is anything on the anvil to show that the future system will be different. But, depositors are safe, no doubt,” he said, adding the government has shown determination in initiating punitive actions, but there is no confidence that they will end up with any convictions.

All punitive actions that are taken do not necessarily or by themselves result in positive outcomes. However, there should be a dual approach of simultaneous punitive action and system improvement, he added.

Reddy elaborated, “the government has shown determination in initiating punitive actions, but there is no confidence that they will end up with any convictions. An important initiative taken in regard to improvement of the system is the law relating to company insolvency. Some preliminary results are appearing.”

He concluded by stating that confidence, coherence, consistency and clarity should be maintained in official pronouncement (read; banking regulator and Government) on banking recognising that banks are special and deposits in banks are very special.

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RBI's inefficiency in controlling banks and its bad governance are the reasons for PSBs bad shape. But the ultimate blame rests on UPA and NDA which miserably failed to save banks and they are the root cause for giving huge loans to few corporates which turned them bad by fraudsters like Mallyah and Niravs. A huge disaster on PSB is awaiting

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Very well and rightly said. Psbs are in a mess because of heavy burden of accumulated bad debts, deteriorating deposits growth and severe mismatch between assets and liabilities. Less said about the Customer Service, the better. The presence of any regulator to take care of service in PSBs is literally absent and banks human resources and Technology do not work in Coordination to say the least. Write off of loans using depositors and tax payers money has been going on with the blessings of authorities and anybody can get away with any wrong doing approach seen in banks' management and accounting jugglaries to cover up even with regulators' approval have made things worst in banks losing the very trust and credibility of public with which banks are run. Sorry state of affairs. Goodie goodie talks cannot be of any solution. Banks Boards Bureau has made the banks non performers and the economy and the people suffer the worst Hope some serious view is taken based on Dr Reddy's observations.

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Deposits in banks are very special indeed as they belong to the people. Whether banks are special, one really doesn't know as many of them almost collapsed already. It is their nationalised status that keeps most PSBs going. In any case there is a public loss in keeping them going as the damage is borne by the tax payers. Better merge them into viable units saving costs on management, staff, infrastructure and overheads. The former RBI Governor's opinion that deposit money is safe and therefore people do not rush to withdraw deposits; however does not reflect the full reality. People simply keep their deposits in PSBs as they do not know any better way of safeguarding the money. Capital adequacy of private banks in comfort zone is a valid assumption only until scams do not surface. Recent happenings in ICICI bank and continued heavy losses by Axis bank have dented the confidence level in private banking also. Recovery of money lost wrongly is the way to keep banks safe and steady

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**Ravi** 22K points

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Accumulated but not disclosed problems were revealed in 2013-14 and subsequently.....So, what does this ex Governor of RBI mean without saying in so many words not withstanding celebrity and media savvy ex Governor of RBI after him? The Governments and RBI prior to 2013-14 were only feigning that things were honky-dory and working for PSBs were fun causing undisclosed misery all around. It looks like we need a Truth Commission.

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