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Merging state banks won't solve governance issue: Former RBI Governor YV Reddy

BY SALONI SHUKLA, ET BUREAU | SEP 06, 2019, 07:43 PM IST

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MUMBAI: Former Reserve Bank of India Governor YV Reddy on Friday said that merging state-run banks will not solve the issue of governance and consolidation should be based on synergies with boards driving the initiative. Reddy also said that global experience has so far shown that half of bank mergers have been ineffective.

“I won't call it a reform, it's a commercial decision based on synergy, global experience in the banking system shows that only half of the bank mergers have been successful,” Reddy said while speaking at the 6th SBI Banking & Economic conclave. “If the purpose is governance, it will not be solved by merging two banks. However, if it's for economies of scale namely operational efficiency it could happen. Mergers could be done by the respective boards as well by analysing synergies, it need not necessarily be through government.”

The government recently merged 10 state-run banks overnight into 4, along with the much-awaited governance reforms that include making PSB managements accountable to respective boards, strengthening the executive succession process and giving longer tenures to top-level directors so that structural changes yield the desired results. The finance ministry's decision comes close to the 50th anniversary of nationalisation of banks and marks 5 years of the PJ Nayak committee set-up to review governance in PSU banks.

Commenting of the collapse of the infrastructure financier IL&FS, Reddy said that the whole episode reflects the failure of risk-assessment capabilities of stakeholders.

“In my view the IL&FS problem reflects the risk-assessment capabilities of large institutions that had exposure to that,” Reddy said. “SBI, LIC should examine this point how did they miss it? It is not a system wide liquidity problem if you ask me it may be a contagion. In a way if the government had to virtually take over IL&FS and run its affairs, it is an indication that the government has recognised it as some sort of a solvency problem.”

What IL&FS leaves in the wake of its destruction is weaker banks, mutual funds, pension funds and an economy which has slowed to a six-year low. With most debating if India is under-going only a cyclical or a more-worrisome structural downturn.

“There is a consensus that current slowdown is a combination of structural and cyclical factors,” Reddy said. “The latest RBI annual report aptly describes the situation that there are large number of uncertainties globally and domestically and they we are in a soft patch. It is said that beauty lies in the eyes of the beholder, the beauty of the Indian economy is also in the eyes of the beholder, it depends who is looking at it half the time.”

Reddy also said that the world is facing enormous uncertainties and it may have geo-political repercussions as well. India could affect the outcomes if it teams-up with some other tier-2 nations. He also painted a grim picture of the on-going trade wars and said that he sees protectionist policies on the rise.

“Tension between globalisation and nationalisation will intensify rather than reduce in the near future,” Reddy said. “The US-China trade war is only the tip of the iceberg there are more fundamental issues at stake. Now, the global currency is the US dollar, China is trying to contest that. In the real sector China is progressing in the financial sector US is dominating, so there is a disconnect.”

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