How to Cite:

Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal

Privatization of Public Sector Banks

Anurag Shukla
M.A Economics
University of Hyderabad

In the Union Budget 2021-22, the finance minister has announced its decision to privatize two Public Sector Banks.Amid government plans to privatize PSB's and opposition arguments against it, let's look at pros and cons of this decision through the journey of Banks in India.

In the first half of 19th century three presidency banks, Bank of Bengal (1806), Bank of Bombay (1840) and Bank of Madras (1843) were established.After the introduction of limited liability in 1860,private and foreign banks entered into the market. In 1921 ,the three presidency banks were merged to create Imperial Bank of India .Apart from doing commercial bank function,the Imperial Bank of India also performed a number of functions which are normally carried out by a Central Bank till 1935.

At the time of Independence there were almost 600 commercial banks operating in the country . However soon after independence, the view that the banks from the colonial heritage were biased in favour of working capital loans for trade and large firms and against small scale enterprises, agriculture and commoners, gained prominence. To ensure better coverage of banking needs of larger parts of economy and the rural constituencies, the Government of India nationalized the Imperial bank which was established in 1921 and transformed it into the State Bank of India (SBI) with effect from 1955.But in 1960s ,it was felt that SBI was not doing enough to cater the needs of small scale industries and agricultural sector.This was partially due to existing ties between commercial banks and industry houses. In July 1969, the Government nationalized all 14 banks whose nation wise deposits were greater than Rs. 50 crores. The bank nationalization in July 1969 led to fulfill its objective to Control the commanding heights of the economy and to meet progressively the needs of development of the economy in conformity with the national policy and objectives.In April 1980,the government took control of another six banks whose nation-wide deposits were above Rs 200 crores and that led to increase in PSBs share of deposits to 92%.

In the period of 1969 to 1991, bank branches in rural areas,leading to financial inclusion , priority sector lending,domestic savings and therefore investment also increased.

1991 Balance of Payment crisis led us to think about the condition of banking in India partially because of IMF conditions. Although bank branches increased but banks remained unprofitable, inefficient and unsound owing to poor lending strategy and lack of risk taking abilities under government ownership.

Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,

How to Cite:

Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal

Privatization -

India went for privatization in the historic reforms budget of 1991, also known as 'New Economic Policy or LPG policy .

Need arisen to Privatise Public Sector Banks.

•Too stringent regulatory requirements of CRR and SLR that required banks to hold acertain amount in government and eligible securities

•Low interest rates charged on government bonds as compared to commercial advances

• Directed and concessional lending

• Administrated interest rates and

• Lack of competition due to monopoly of PSBs.

A high-level committee was constituted under the chairmanship of Shri. M. Narasimhan (Committee on Financial System or Narasimham Committee - I and II) to review the progress and working of the Indian financial sector and to suggest measures to reform it .

Recommendations:

•Autonomy in Banking: Greater autonomy was recommended for public sector banks to function with equivalent professionalism.

•The committee recommended Government equity in nationalized banks to be reduced to 33% for increased autonomy.

•The committee recommended the merger of large banks to make them strong enough for supporting international trade.

•Capital adequacy norms should be raised by government.This would increase their risk-taking ability.

•Most of the reforms as recommended by the Narsimhan committee have now been implemented.

•The Nachiketmor committee (2013)also talked about financial inclusion.

•P J Nayak committee suggested bringing down government stake in public sector banks to below 50%.

Issues with Public Sector Banks:

•NPA's:

Non-Performing Assets (NPA) are loans that the borrower fails to pay back to the bank, further high levels of NPAs erode a bank's profitability.

• Most PSBs are also unable to maintain a capital adequacy ratio.

• In the case of many PSBs, the RBI had to restrict the normal functioning of the banks — this is referred to as the banks being put under Prompt Corrective Action (or PCA) — and forced them to improve their financial performance metrics before being allowed to resume normal banking activities.

•Losses in Rural Branches:

Most of the rural branches are running at a loss because of high overheads and the prevalence of the barter system in most parts of rural India.

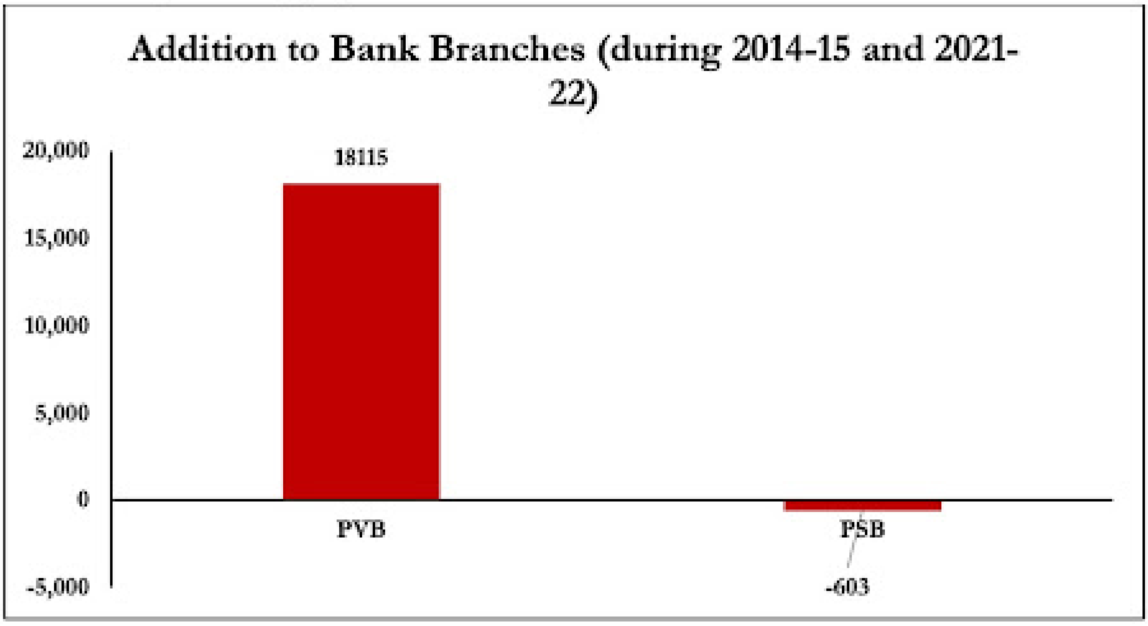
• Bureaucratisation:

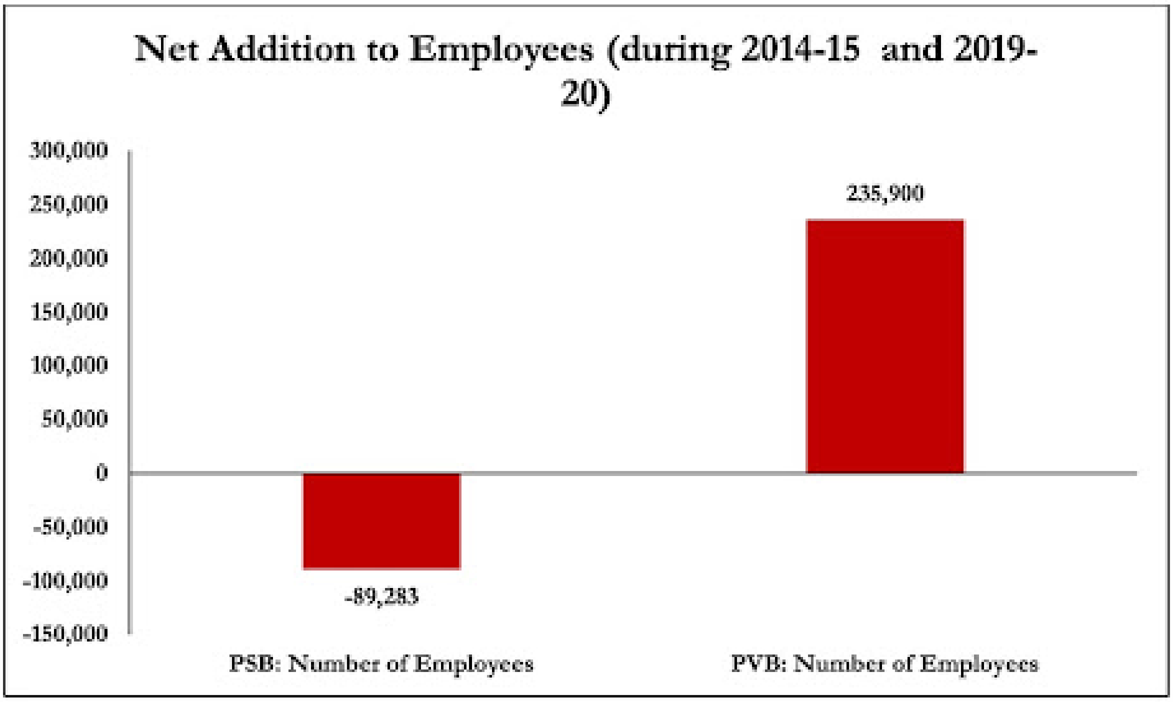
Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,

How to Cite:

Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal

The Change in Employment and Bank Branches in PSBs and Private Banks





RBI, Handbook of statistics on Indian Economy, Money and Banking, Bank Group wise distribution of Employees of Scheduled Commercial Banks.

The smooth functioning of banks has been hampered by red-tapism, long delays, lack of initiative, and failure to take quick deci-sions.

Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,

How to Cite:

Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal

• Financial Burden to Government:
Rather than wasting taxpayers' money to recapitalise PSBs, the government should simply sell them off to the private sector.
This would reduce the financial burden on the government while also ensuring that PSBs become more efficient and profit-making entities under private ownership.

Efficient Performance of Private Sector Banks:
•Efficient:
The Private sector Banks (PVBs) are far more efficient, far more productive, and far less corrupt than the PSBs.

• Less Amount of NPA:
Private sector banks have lower gross NPAs.

• Enhanced Banking Facilities:
They provide a more significant contribution towards extending loans and a higher percentage of contribution to getting deposits from savers.

•More Branches and More Jobs:
They created more branches and new jobs while the public sector banks saw declines on both counts.

•Fetches More Market Value:
When the Economic Survey reviewed bank nationalization in 2020, it was found that every rupee of taxpayer money invested in PSBs fetched a market value of just 71 paise. This is called the market to book ratio.
In stark contrast, every rupee invested in new private sector banks fetches a market value of Rs 3.70. In other words, private banks give more than five times more value than PSBs.

PSBs Vs private sector banks:who is more efficient?

•Financial inclusion

Public sector banks are more financially inclusive than private sector banks courtesy to schemes like PM JAN DHAN YOJANA,which envisages universal access to banking facilities .
Public Sector Banks provide 36.2 crore beneficiaries while Private sector banks accounted for just Rs 1.3 crores of the total of almost Rs 46 crore beneficiaries.
While the private banks dominate the metropolitan areas, it is the public sector banks that operate branches in rural India.
PSBs provide more ATMs in rural India.

Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,

How to Cite:
Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal

Efficiency –

When profit maximization is the sole motive, efficiency of the Private sector banks has always surpassed that of their public sector counterparts.
However, when the objective function is changed to include financial inclusion—like total branches, agricultural advances and Priority Sector Lending advances— PSBs prove to be more efficient than Private sector banks.

Formar NITI AAYOG VC Arvind Pangaria along with Poonam Gupta ,NCAER in a research paper advocated about privatization of PSBs into private sector banks.According to Arvind Pangaria,pSBs are lagged behind the Private banks in all major indicators, namely;
•Larger NPAs
•Higher operation costs
•Lower returns on assets and equity.
They made a solid pitch for privatization of PSBs -
1) Superior performance of private banks.
2) Presence of PSBs potentially destabilizes private banks (evident during global financial crisis 2008-09)
3) Government ownership of banks gives rise to many governance issues bearing on both the efficiency of PSBs operations and ability of RBI to regulate the sector.
4) Government ownership brings with it political interference through the flow of loans to serve political objectives.
5) Regular bailouts of PSBs cost taxpayers vast sums of money.

Arvind Pangaria suggested to privatize all Public sector banks to private banks except SBI.

Way Forward

•There is a need for a nuanced approach and further, members of RBI's Banking Research Division have warned against the conventional perspective of viewing privatization as a panacea for all ills.
•The big bang approach of privatization of the public sector banks may do more harm than good as the repercussions could lead to the vulnerable population losing their financial inclusion and further making it difficult for them to access banking and related facilities.

A report by RBI on Privatization of Public Sector Banks: An Alternate Perspective'
Some of the major highlights of this report are:

1) While private sector banks are more efficient in profit maximization, their public

Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,

How to Cite:
Anurag Shukla (Nonember 2022). Privatization of Public Sector Banks
International Journal of Economic Perspectives,*16*(7),152-157
Retrieved fromhttps://ijeponline.com/index.php/journal
sector counterparts have done better in promoting financial inclusion.

2) Labour cost efficiency is higher in PSBs in comparison to Private Sector Banks.

3) Empirical evidence suggests that lending by PSBs is less procyclical than Private Sector Banks. Thus, PSBs help counter-cyclical policy actions to gain traction.

4) The gradual approach to privatization adopted by the government can ensure that a void is not created in fulfilling the social objective of financial inclusion.

Banks are essential to the expansion of the economy. In India, the economy and its stakeholders have been ignored by the banking system, which is dominated by public sector banks (PSBs). Despite numerous policy changes over the previous ten years, PSB's underperformance has persisted. Private banks, meanwhile, have significantly increased their performance and market share. Although under this new system, the State Bank of India (SBI) stay under Government control for the time being due to its greater performance and adherence to the development view of the PSBs, overall, privatization of banks is a vital step as this may help strengthen the banks performing well, while on the other hand, it may assist underperforming banks in performing better due to bank privatization.

References:

1) Report of the committee on the Financial System 1991.(NARASIMHAM COMMITTEE)

2) INDIAN ECONOMY by Gaurav Datt and Ashwani Mahajan,72nd edition

3) Union Budget speech, 2020-21

4) Indian Economy by Vivek Singh,5th edition

5)Privatization of Public Sector Banks in
India: Why, How and How Far. A research paper by POONAM GUPTA AND ARAVIND PANAGARIA.

6) Privatization of Public Sector Banks: An Alternate Perspective, RBI bulletin August 2022.

Submitted: 27 July 2022, Revised: 09 August 2022, Accepted: 18 August 2022, Published: Nov 2022,