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Syllabus: GS-3-> Indian Economy

'Bank consolidation is a necessary step to curb the rising NPA issue but not sufficient'. Comment.

First read: [Problem of rising NPA](#)

Why in news?

- The government recently proposed the amalgamation of state-owned Bank of Baroda (BoB), Dena Bank and Vijaya Bank.

How did the idea take shape?

- A committee headed by former RBI Governor M Narasimham was appointed in 1991.
- It is more than 27 years since it had recommended a restructuring of Indian banks.
- It made the first call for pruning the number of government-owned banks which was over two dozen.
- It recommended having three or four large banks including State Bank of India that could be positioned as global banks.

- Besides, there can be eight to ten with a national footprint or presence.
- In 2016, the government decided to pursue consolidation after first pumping in more capital.
- This is to put back on track many banks weighed down by a huge pile of bad loans.
- To facilitate this, the government last year put in place an Alternative Mechanism on bank mergers.
- By this, an inter-ministerial panel was to be set up to supervise merger proposals and approve them.
- The first such proposal is the recent Bank of Baroda (BoB), Dena Bank and Vijaya Bank consolidation.

Why the amalgamation?

- It has been recognized for long that having several banks that are majority-owned by the government was not a sensible strategy.
- It's because they virtually do the same business, and compete for the same set of customers.
- It also meant a lower return on the capital employed by the government.
- There are other factors as well to be taken into account, including -

1. Changing face of banking marked by technological changes
2. Challenges to raising capital that the owner (the government) has to provide periodically
3. The need for consolidation in the sector
4. Putting an end to fragmentation

- The government is also emboldened by the experience of the merger of five subsidiaries of the State Bank of India last year.

How is it going to benefit?

- The amalgamation will create India's third-largest bank.
- It would take form as a business of Rs 14.82 lakh crore and over 9,600 branches across the country.
- Mergers are often advocated on the basis of synergies.
- These could be in terms of operational efficiency with a large pool of staff in a merged entity.
- It could help boost business, expand reach and offer more services or products.
- On a standalone basis, Vijaya Bank had strength in the South.
- On the other hand, Bank of Baroda and Dena Bank had a stronger base in Western India.
- This would mean wider access for both the proposed new entity and its customers.
- Besides, the move will lead to a lower NPA (non-performing assets) ratio for the new bank.
- The NPA ratios are now 11.04% for Dena Bank, 5.4% for Bank of Baroda and 4.1% for Vijaya Bank.
- This could, in turn, mean lower capital requirements from the government.
- The new bank, with its higher capital base (12.25 %) can have better ability to lend more.

What are the issues?

- The boards of all three banks, being public listed entities, will meet soon and try and get approval for the government proposal.
- This will not be a challenge as the government has the dominant shareholding in all the three.
- The real challenge is the integration in a new entity, whether in operations or culture.
- It helps that the three banks chosen have a common technology platform.
- This may make it work like in the case of the SBI and its subsidiaries.
- However, human resources can often be a challenge with contrasting HR practices.
- Also, aligning these with employee expectations or aspirations will also test the new management.

- The other major test will be leadership i.e. choosing one of the CEOs to head the new bank and with a reasonable tenure.
 - Besides, addressing the concerns of unions and shareholders will be another significant task.
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