

Chapter 1

Introduction

1.1 Over the last several years, the Government of India and the Reserve Bank of India have been seized of the problem of weakness that has gripped some parts of the banking system. This weakness became apparent in the early 1990s when, following introduction of internationally accepted prudential accounting norms, banks were required to segregate their performing and non-performing assets and, after providing for those which are non-performing, build up a minimum level of capital related to risk-weighted assets.

1.2 Public sector banks have so far been able to meet their requirements of additional capital by infusion of funds by the Government of India or by accessing the markets. With the exception of a few, most public sector banks had to rely exclusively on the Government of India for their capital requirements. There have been some among them who have had to be provided with additional capital repeatedly. The quantum of such capital infusions by the government has often been quite large.

1.3 Save in a few cases wherein additional capital was needed to support the growing volume of business, the need for repeated capital infusion is on account of chronic weaknesses which, as discussed elsewhere in this report, have been caused by several factors, both internal and external. However, a stage has now been reached where further efforts at restructuring some of these banks cannot be confined merely to infusion of capital and giving certain targets for improvement in performance. One would necessarily need to look into their ability to achieve a minimum level of competitive efficiency in order that their operations become profitable on a sustainable basis. Any effort at their restructuring will have to involve operational as well as financial restructuring. Operational and organisational paradigms within which these banks are functioning will have to be revised and deficiencies that have got built into their working removed.

1.4 It was against the above background that the Reserve Bank of India, in consultation with the Government of India, set up the present Working Group under the chairmanship of Shri M.S. Verma, former Chairman, State Bank of India, and presently Honorary Adviser to the Reserve Bank of India, to suggest measures for revival of weak public sector banks. A copy of the letter dated 6 February 1999 addressed to Shri Verma in this regard is at Annex 1. The Working Group had the following members:

- i. Shri K.R. Ramamoorthy, Chairman, Vysya Bank Ltd.
- ii. Shri M.M. Chitale, Chartered Accountant (former President, Institute of Chartered Accountants of India).
- iii. Shri P.K. Choudhury, Managing Director, Investment Information and Credit Rating Agency of India (ICRA Ltd.).
- iv. Shri J.R. Prabhu, former Executive Director, Reserve Bank of India.
- v. Dr. Sushil Chandra, former Director, International Management Institute, New Delhi.

Shri C.R. Muralidharan, General Manager, Reserve Bank of India, Department of Banking Operations and Development, Central Office, was the Member Secretary.

1.5 The terms of reference of the Working Group were as under:

- a. Criteria for identification of weak public sector banks;
- b. To study and examine the problems of weak banks;
- c. To undertake a case by case examination of the weak banks and to identify those which are potentially revivable;
- d. To suggest a strategic plan of financial, organisational and operational restructuring for weak public sector banks.

1.6 The Working Group was expected to submit its report by 30 June 1999. The Group, however, felt that with the financial results of most

of the public sector banks for the year 1998-99 becoming available by the end of June 1999, it would be desirable to analyse them, with particular reference to the position of their NPAs, and suitably adjust the restructuring strategies. Since one of the banks concerned could finalise its balance sheet only by the end of July 1999, the date for submission of the report had to be extended to the middle of August 1999 with the concurrence of Reserve Bank of India.

Working Group's Methodology

1.7 The Working Group's method of work primarily comprised of a detailed examination of the published and other financial and operational data of all the public sector banks. For looking closely into the working, information/data was called for from all public sector banks and conclusions have been drawn on the basis of information received as also their balance sheets and other published figures. For recent data, the Group has relied upon data being collected by the Reserve Bank of India on an ongoing basis as part of its off-site monitoring of banks.

1.8 The Working Group sent questionnaires to the three identified banks eliciting certain information and their views on a wide range of operational issues. This formed one of the bases for the Working Group to formulate its views on the present state of health of these banks and possible strategies for their restructuring aimed at restoring their competitive efficiency. A copy of the questionnaire is given at Annex 2.

1.9 Since the work involved in the detailed examination of the functioning of the three clearly identifiable weak banks, viz., Indian Bank, UCO Bank and United Bank of India, was going to be quite voluminous and keeping in view the limited time available to it, the Working Group deemed it appropriate to constitute three sub-groups for studying each of the three identified banks. Each of the three sub-groups was assisted by a specialised agency with expertise and experience in studying problems related to weak units. Details of the constitution of the sub-groups are given in Annex 3.

1.10 The sub-groups were required to pinpoint the causes of

weakness and examine whether the three identified banks have the inherent ability and a viable plan to get over the problems and operate as banks with minimum competitive efficiency. The reports of the sub-groups, in a sense, form part of this report even though the Working Group, with a larger picture in view, has in some cases gone beyond their specific recommendations. The executive summaries of the three sub-group reports are given at Annexes 4 to 6.

1.11 The Working Group held a series of meetings among its members, with the sub-groups referred to above and with various senior officials of the Government of India, Reserve Bank of India and the three identified banks. It also met with and benefited from the views of a cross-section of people connected in various ways with banking. These included Chairmen/CEOs of Indian and foreign commercial banks and financial institutions, the Board for Financial Supervision, the Chief Vigilance Commissioner and a number of independent observers. A list of persons with whom the Working Group interacted is given at Annex 7.

1.12 The Working Group also met with, during various stages of its work, representatives of unions/associations. The representatives of the United Forum of Bank Unions also made a presentation to the Working Group. They gave their views as to the reasons for the present predicament of the weak banks and suggested what in their opinion could be the remedial measures.

Outline of the report

1.13 Chapter 2 takes a look at the international experience with regard to bank restructuring insofar as they are relevant to the Indian context. An overview of the public sector banks, based on the findings of the Working Group, is given in Chapter 3. This chapter also discusses the definition of weak banks the Working Group has adopted and the manner in which it has been applied to identify the weak public sector banks. The factors contributing to weakness of the banks are delineated and discussed in detail in Chapter 4. The past efforts at restructuring these identified banks and the results thereof are discussed in Chapter 5. Chapter 6 goes into the

present position of the weak banks based on the reports of the sub-groups and the financial results for the year 1998-99. The Working Group's recommendations regarding the restructuring strategy to be adopted for the three identified weak banks are detailed in Chapter 7. A summary of recommendations has been furnished in Chapter 8.

Acknowledgements

1.14 The Working Group would like to place on record its appreciation of all support and assistance that was provided to the Working Group by the Government of India, Reserve Bank of India, various banks and other institutions. The Governor and the Deputy Governors of the Reserve Bank of India were kind enough to spare their valuable time on more than one occasion to interact with the Working Group and offer it their wise guidance.

1.15 The Working Group also had the benefit of drawing from the deep insight, experience and expertise of several eminent persons who, as thinkers and practitioners connected with the world of banking and finance, shared their views with the Working Group. The Working Group is grateful to them for their valuable contribution.

1.16 The Working Group would also like to thank the CMDs, EDs, other senior officials and the respective officers and staff unions of all the three identified banks for their co-operation. Thanks are also due to the regional offices of the Reserve Bank of India at Calcutta, Chennai and New Delhi for their warm hospitality during the visits made by the Working Group and the sub-groups.

1.17 The work of the sub-groups would not have been concluded in time but for the excellent service rendered to it by the three institutions identified to assist them. These institutions were ICRA Ltd. which assisted in the study of Indian Bank, SBI Capital Markets Ltd. for UCO Bank and CRISIL for the United Bank of India. In particular, thanks are due to S/Shri R. Raghuttama Rao, V. Sriram and N. Mahesh of ICRA Ltd., Kishore Gandhi, George Mathew, N. Shankar and Pathik Gandotra of CRISIL, and Ms. Anjali Gupta of SBI Capital Markets Ltd.

1.18 The Working Group received very valuable contribution from Shri C.R. Muralidharan, who was the Member Secretary, Ms. Sudha Damodar, Deputy General Manager, Shri G. Sreekumar, Assistant General Manager and Shri N. Badri Prasad, Assistant Manager, all from the Reserve Bank of India. Ms. Lakshmi Sundararajan, Private Secretary, Ms. Priya Raut and Ms. Beena Nair, also from the Reserve Bank of India, assisted the Working Group in its work. The Working Group would like to record its appreciation and thanks for the assistance rendered.