Bad Debt and Public Ownership*

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The semi-annual Financial Stability Report from India's central bank signals that India's banking system, especially the public banking system, has put behind it the stress from disturbingly high non-performing or bad loans on its books. The story as officially told is now familiar. As a result of "aggressive lending practices" and "wilful default/loan frauds/corruption in some cases", stressed assets in the banking system rose sharply along with a rise in aggregate gross advances of public sector banks (PSBs)from Rs. 16,98,570 crore at the end of March 2008 to Rs. 45,90,570 crore at the end of financial year 2014. Since this is being routinely reported in answers to parliament questions during the NDA regime, the choice of end date—the installation of the first Modi government—does seem convenient. But it is also justified because the decision of the Reserve Bank of India (RBI) to mandate an asset quality review to address massive underreporting of non-performing assets (NPAs) was taken in 2015. In that year the RBI took cognisance of the fact that through restructuring agreements that were neoliberal by design, non-performing assets (NPAs) had been reclassified as restructured assets and temporarily concealed from public view. The asset quality review resulted in an increase in the volume of recorded gross NPAs of PSBs from Rs. 2,16,739 crore on 31 March 2014 to Rs. 8,45,475 crore on 31 March 2018, or from 4.72 per cent of gross advances to 15.52 per cent of gross advances, according to figures in the answer to Rajya Sabha starred question No 355 on 5 April 2022.

But the picture has changed considerably since. Remarkably, the RBI now reports that as on 30 September 2022, the gross NPA ratio of public sector banks has declined to just 6.5 per cent, bringing the figure within striking range of its 2014 value. The Financial Stability Report of a year earlier, released by the RBI in December 2021, had projected in its baseline scenario that the gross non-performing assets ratio of all scheduled commercial banks (SCBs), could increase to 8.1 per cent by September 2022. Even the public banks that carried much of the NPA burden have now brought it down to a far lower figure. That is quite an achievement given the impact on banking performance of the pandemic and of the debt payment moratoriums and special credit lines announced by the government in response to the pandemic in 2020. That the turnaround could be managed in this environment establishes that the assessment that the government would not be able to save the banks on its own, necessitating large scale mobilisation of capital from the markets, especially through disinvestment or privatisation, was unfounded.

The strategy of addressing the bad debt problem had many components. Recognition had to be followed by provisioning to cover for the losses expected. According to an answer to Rajya Sabha question No. 1507 dated 20 December 2022, public sector banks had made provisions totalling Rs. 21,48,906 crore over the five year period ending 31 March 2022. This not only resulted in losses for the banks, but also ate into the capital of the banks that had to be reconstituted to ensure that the specified minimum capital adequacy ratio was maintained, and solvency ensured. One way in which this was done was of course through direct recapitalisation by the government, by subscribing to bank equity from its own fund or funds mobilised by issuing recapitalisation bonds to the banks themselves. According to the answer to the question cited earlier, the government had infused Rs. 2,86,043 crore into PSBs over the five year period ending 2021-22. That equals around 13 per cent of the provisions made by the PSBs over those years and 34 per cent or a third of the NPAs of the PSBs as on 31 March 2018. This helped, but clearly it was not just recapitalisation that has retrieved the PSBs out the mess they seemed to be in in 2018.

Direct mobilisation of capital by banks played an even smaller role, with capital mobilised by the public sector banks over the four financial years ending March 2019 placed at just Rs. 65,800 crore. And very little of this was through the sale of equity to private parties. As at the end of March 2022, ownership of the RBI and the government in 12 public sector banks varied from 57 per cent to 98 per cent and the combine holding of the government, the RBI and resident financial institutions from 76 to 99 per cent. Privatisation has not moved forward and Indian banks are still overwhelmingly state-owned institutions. This is not surprising since, while there was persistent talk of the need to privatise public banks to mobilise resources for recapitalisation following NPA reduction, it was clear that private investors would have little interest in buying into banks that were burdened with debt.

A number of other initiatives played a role in NPA reduction. Given the uneven distribution of NPAs across banks and the particularly bad balance sheet position of some of them, consolidation of weak with stronger banks was a measure that was adopted. Vijaya Bank and Dena Bank were amalgamated with Bank of Baroda in April 2019 and Oriental Bank of Commerce and United Bank of India were amalgamated with Punjab National Bank, Andhra Bank and Corporation Bank with Union Bank of India, Syndicate Bank with Canara Bank, and Allahabad Bank with Indian Bank, with effect from April 2020.

Moreover, public banks were mandated to write off bad debt after provisioning for them. NPAs which have been fully provisioned for were written off after four years of being identified. According to the RBI, over the five financial years ending March 2022, scheduled commercial banks, especially PSBs, wrote-off bad debt totalling Rs. 10,09,511 crore. In principle, borrowers remain liable for repayment of 'technically' written-off loans and the process of recovery of dues from borrowers is supposed to continue. However, little has actually been recovered in practice. Thus, recovery proceedings through a host of channels—suits in civil courts or in Debts Recovery Tribunals, action under the SARFAESI Act, cases 'resolved' under the Insolvency and Bankruptcy Code, sale of non-performing assets through Asset Reconstruction Companies, and resolution through negotiated settlement or compromise—have not yielded much by way of recovered dues from written off loans. As opposed to the more than Rs. 10 lakh crore of written-off debt over the five years ending March 2022, that recovered by the commercial banks during that period was just Rs. 1,32,036 crore or around 13 per cent. Clearly, suffering the pain of providing for bad loans and writing them off with limited recovery was the principal means by which public sector banks have managed to bounce bank, reporting profitability that is significant in recent quarters.

In sum, despite statements by RBI officials, government spokespersons, and 'experts' from the NITI Ayog and other think tanks, that privatisation was the means to resolve the bad debt problem, public sector banks have addressed the issue without handing over ownership of significant blocks of shares to private players, who in any case were not interested in buying into NPA-burdened banks. And this they did with limited direct support from the government. It is no doubt true that in this process of resolution, big business players have been beneficiaries, getting away lightly, having taken on and not repaid huge debts and, barring those identified as wilful defaulters, not even being named individually for the malfeasance. But that failure did not prevent the PSBs from cleaning their balance sheets, reviving credit growth and improving profitability.

What is intriguing is that even with such a resolution process nearing satisfactory completion the call for disinvestment and privatisation continues. The Finance Minister's budget speech for financial year 2021-22 declared that the government intends to privatise two PSBs. A paper by two ostensibly 'independent' experts, one of whom has served as Vice Chairperson of Niti Ayog, calling for privatisation of all public sector banks, excepting for the State Bank of India, is receiving much attention in policy circles. While bank privatisation or denationalisation could not be carried out using NPAs as an excuse, the demand for it seems to intensify as the books of banks are cleaned up. This is worrying. If public banks were not attractive targets for private acquisition when NPAs on their books were large, they have turned attractive with comfortable balance sheets, rising profits and large volumes of safe government bonds on their books. It cannot be doubted that the NPAs carried by public banks had to be cleaned out. But the evidence after that task has been completed of the call for privatising these banks gathering momentum, suggests that the government's push to complete the resolution process in record time possibly had a different motivation. That motivation seems to be the cleaning of bank books to pave the way to implementing a central objective of its neoliberal agenda—the reversal of bank nationalisation.

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