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INDIA'S LARGE ECONOMY NEEDS AN EFFICIENT BANKING SECTOR TO SUPPORT ITS GROWTH; STATE OF THE BANKING SECTOR IN INDIA NEEDS URGENT ATTENTION: ECONOMIC SURVEY

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Ministry of Finance

India's Large Economy Needs an Efficient Banking Sector to Support its Growth; State of the Banking Sector in India Needs Urgent Attention: Economic Survey

Enhancing Efficiency of PSBs Through Fin Tech is the Way Forward: Survey

Economic Survey Proposes Creation of Fin tech Hub for PSBs – the Public Sector Banking Network (PSBN)

Part-Ownership of PSBs by Employees Through Employee Stock Option Plans Will Reduce Agency Problems: Survey

Financial Inclusion, in Large Part, Happened in August 2014 Through the Pradhan Mantri Jan Dhan Yojana (PMJDY): Survey

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Public Sector Banks (PSBs) with about 70 per cent of the market share in Indian Banking have an onus of supporting the Indian economy and fostering its economic development. The Economic Survey 2019-20, tabled by the Union Minister for Finance & Corporate Affairs, Smt. Nirmala Sitharaman, in Parliament today, observes that there is disproportionate dwarfism of the Indian banks when compared to the size of the Indian economy. For India to march in its goal of becoming a $5trillion economy, PSBs – the dominant banks in our banking system – need to become efficient. The economy needs PSBs to perform to their fullest potential and support economic growth rather than pullback lending, which has a detrimental effect on growth and welfare.

The Survey expresses that if Indian banks were proportionately large in relation to the size of the Indian economy, India should have at least six banks in the global top 100 than just the current largest PSB- State Bank of India (SBI)-which is the 55th largest bank globally.

The survey notes that despite nationalisation a significant portion of the poor remained unbanked till 2014. Financial inclusion, in large part, happened in August 2014 through the Pradhan Mantri Jan Dhan Yojana (PMJDY), the first week of which saw more than 18 million bank accounts – a record in the Guinness Book of World Records.

Digital Transactions & DBT:

The Economic Survey notes that the growth in digital transactions has been significant. The use of direct benefit transfers has increased exponentially over the last five years, has helped to bring both credit and deposits into the banking system across all geographies (rural, semi-urban, urban and metropolitan). The high elasticities across all geographies clearly demonstrate the opportunity that exists for Indian banks to benefit from the greater use of DBT by the Government. There are possibilities for the Indian banking sector to grow proportionate to the scale of the Indian economy. The new programmes have resulted in a surge of individuals and businesses being brought into the formal economy. Perhaps more important is that the inclusion is backed by state-of-art digital infrastructure that generates and stores an abundance of high quality structured data on the all aspects of the economic lives of firms and individuals. Such data are, of course, the gold mine for economic growth in the 21st century. They offer essentially unlimited and uncharted possibilities, especially for firms and individuals who have been traditionally excluded from the financial system.

Enhancing efficiency of PSBs: the way forward

The Economic Survey also observes that over Rs. 4,30,000 crores of taxpayer money is invested as Government's equity in PSBs. In 2019, every rupee of taxpayer money is invested in PSBs, on average, lost 23 paise. The state of the banking sector in India, therefore, needs urgent attention.

With the key drivers of India's growth prospects - a) highly favourable demographics – with 35 per cent of its age; (b) a modern and modernising digital infrastructure that encompasses the "JAM" trinity viz., the PMJDY bank account programme, the Aadhaar unique identification programme, and the mobile phone infrastructure; and (c) a uniform indirect taxation system (GST); India's growth path depends on how quickly and productively these growth levers are deployed using a well-developed financial system. These growth opportunities position PSBs well to utilise FinTech like Credit analytics using Artificial Intelligence and Machine Learning (AI-ML).

Creation of FinTech Hub for PSBs: The Public Sector Banking Network (PSBN)

The Survey proposes that PSBs need to embrace FinTech, which is revolutionising the global financial landscape. FinTech has radically changed the way information is processed by banks. The Economic Survey observs that a large proportion of NPAs of Indian banks, especially PSBs, could have been prevented if data and analytics were employed in corporate lending and that a robust credit analytics platform could have easily picked up and provided warning signals besides curbing double-pledging of collateral.

The survey proposes establishment of a GSTN like entity, called PSBN (PSB Network), to use technology to screen and monitor borrowers comprehensively and at length. Apart from utilising data from all PSBs, which would provide a significant information advantage, PSBN would utilize other Government sources and service providers to develop AI-ML ratings models for corporate. Better decision making on credit underwriting would reduce the burden of NPAs, apart from helping them in fraud prevention. The high operating costs of each PSB would decrease by helping them automate the end-to-end process of lending. PSBs would be able to make quicker decisions, process loan applications faster, and reduce turn-around-times (TAT).

The survey proposes to enable employees to become owners in the banks and thereby incentivise them to embrace risk-taking and innovation continually, a portion of the government stakes can be transferred to employees exhibiting good performance across all levels of the organisation through Employee Stock Option Plans (ESOPs). Part-ownership of PSBs by employees will reduce agency problems. Benefits include the possible change of the mind-set that of an employee to that of an owner. Employees can constitute one of the blocks of new owners of PSBs through an employee stock ownership Plan (ESOP) that is conditioned on employee performance. Ownership by motivated, capable employees across all levels in the organisation could give such employees tangible financial rewards for value enhancement, align their incentives with what is beneficial to the PSB, and create a mind-set of enterprise ownership for employees a long-term solution to case for employee stakes in PSBs.

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