Draft Scheme of Amalgamation of PMC & USF Bank: RBI

Why in News

Recently, the **Reserve Bank of India (RBI)** released a draft scheme of amalgamation of **Punjab and Maharashtra Cooperative (PMC) Bank** and **Unity** Small Finance Bank **(USF).**

- Earlier, **PMC was put under restrictions on account of fraud** that led to a steep deterioration in the networth of the bank.

Key Points

- **About:**
  - According to the draft scheme of amalgamation, following the amalgamation, **depositors of PMC Bank will get their money back over a period of 3-10 years.**
  - The **interest on any interest-bearing deposit with the transferor (PMC) bank will not accrue** after 31st March 2021.
- **Significance:**
  - The **takeover of assets and liabilities of PMC Bank, including deposits, by Unity, will give a greater degree of protection for the depositors.**
    - **USF Bank is being set up with capital of about Rs 1,100 crore as against a regulatory requirement of Rs 200 crore** for setting up a small finance bank under the guidelines for on-tap licensing of small finance banks in the private sector.

Merger of Banks

- **About:**
  - In a Merger, banks are benefited in combined business operations and ventures. Together they are able to increase shareholder value and cater the needs more effectively.
  - Bank consolidated procedures are provided under the **Banking Regulation Act,1949. Section 45** in the act empowers RBI to apply to the Central Government for suspension of business by a banking company and to **prepare a scheme of reconstitution of amalgamation.**
- **Recent Examples:**
  - In 2019 the Finance Minister announced the biggest consolidation plan of **Public sector Banks (PSBs)- merging 10 of them into just 4.**
  - In January 2019 Cabinet Committee on Economic Affairs (CCEA) approved the merger of state-run **Vijaya Bank, Bank of Baroda and Dena Bank.**
  - In April 2017, **5 associate banks were merged with SBI** – State Bank of Bikaner and Jaipur, State Bank of Hyderabad, State Bank of Travancore, State Bank of Mysore and State Bank of Patiala.
  - Government also initiated **amalgamation of** Regional Rural Banks under Phase 3

consolidation, bringing them down from 56 to 38.

- **Benefits:**
    - **Competitive:** The consolidation of Banks helps in strengthening its presence globally, nationally and regionally.
    - **Capital and Governance:** The government's intention **is not just to give capital but also give good governance.** The financial system of the enlarged institution will be more profitable and protected.
        - The lending capacity of the banks will increase and their balance sheet would also be strong.
    - **Efficiency:** It has the **potential to reduce operational costs d**ue to the presence of shared overlapping networks. And this enhanced operational efficiency will reduce the lending costs of the banks.
    - **Technological Synergy:** All merged banks in a particular bucket share common **Core Banking Solutions (CBS)** platform synergizing them technologically.
    - **Self-Sufficiency:** Larger banks have a **better ability to raise resources** from the market rather than relying on State exchequer.
    - **Monitoring:** With the number of Banks coming down after the process of merger – capital allocation, performance milestones, and monitoring would become easier for the government.
- **Challenges:**
    - **Decision Making:** The banks that are getting merged are **expected to see a slowdown in decision making** at the top level as senior officials of such banks would put all the decisions on the back-burner and it will lead to a drop in credit delivery in the system.
    - **Geographical Synergy:** During the process of merger, the **geographical synergy between the merged banks is somewhat missing.** In three of the four merger cases, the merged banks serve only one specific region of the country.
        - However, the merger of Allahabad Bank (having a presence in the East & North region) with the Indian Bank (having a presence in South) increases its geographical spread.
    - **Slowdown in Economy:** The move is a good one but the timings are not just apt. There is **already a slowdown in the economy**, and private consumption and investments are on a declining trend. Hence, **there is a need to lift the economy and increase the credit flow** in the short-term, & this decision will block that credit in the short-term.
    - **Weak Banks:** A complex merger with a weaker and under-capitalized PSB would **stall the bank's recovery efforts** as the **weaknesses of one bank may get transferred** and the merged entity may become weak.

Source: IE