

Chapter IV

Monitoring Capital Infusion in PSBs

Significant capital has been infused in the PSBs in the past decade by DFS (amounting to ₹ 1,18,724 crore over 2008-17). Audit reviewed the mechanisms available to DFS for monitoring the effect of capital infusion in PSBs over the same period. It was noticed that DFS communicated targets to PSBs essentially through Statements of Intent (SOI) and Memorandum of Understanding (MoU). Audit reviewed these documents (to the extent they were made available to Audit²⁰) and the processes in DFS for monitoring capital infusion in PSBs.

4.1 Statement of Intent

The mechanism of SOI on Annual Goals to monitor the performance of PSBs, was introduced on the directions (June 2005) of the Ministry of Finance. A set of performance parameters were defined and targets were set for the PSBs against these parameters. SOI parameters have been revisited and redrafted from time to time, with amendments on 23 April 2010, 21 October 2011 and 20 May 2012. Post the amendment of May 2012, there were 44 SOI parameters which were to be monitored by DFS. Besides being a tool for monitoring performance of PSBs, the SOIs are also used to incentivize their top management when the SOI targets are achieved.

4.1.1 Mismatch of SOI targets vis-à-vis targets set for sanction of additional capital

Audit noticed that in one year (2010-11) out of the nine years (2008-17) reviewed, conditions were stipulated in the sanctions that were issued for infusion of capital in PSBs. No such conditions were on record for the other years. Based on the documents made available, Audit noticed that the targets stipulated against specific parameters at the time of sanction of capital in 2010-11 were significantly different from the targets set for the same parameters in the SOI for the same period in case of five PSBs. The mis-match in the two sets of targets and the actual achievements in these PSBs is tabulated on the next page:

²⁰ SOI documents for 2011-12, 2012-13, 2013-14 and 2014-15 were made available to Audit. MoUs signed in February/ March 2012 were also provided

Table 4.1: Mis-match in the two sets of targets and the actual achievements in these PSBs

Parameter	2010-11			2011-12			2012-13		
	Target along with Sanction (per cent)	SOI Target (per cent)	Achievement (per cent)	Target along with Sanction (per cent)	SOI Target (per cent)	Achievement (per cent)	Target along with Sanction (per cent)	SOI Target (per cent)	Achievement (per cent)
Bank of Maharashtra									
ROA	0.80	0.70	0.47	1.00	0.55	0.55		0.70	0.74
Direct Agri. Adv	11	10.50	9.93	12.5	10.27	10.43	13.50	11.00	11.22
Adv. To Weaker Sections	7.50	7.00	6.49	9.00	6.72	6.72	10.00	8.00	8.31
Gross NPA (per cent)	2.40	2.60	2.47	2.00	2.36	2.28		2.48	1.49
Net NPA (per cent)	1.30	1.50	1.32	1.00	1.30	0.84		1.22	0.52
Net Profit (₹ in crore)	Min growth of 20 per cent p.a	485	330		400	430.83		650	759.52
Cost Income Ratio	Improve 200 bps p.a till 40 per cent	56	65.79		59	52.02		52	45.54
UCO Bank									
CASA Deposits	Improve 5 per cent p.a till 30 per cent	N.A	23.20		30	23.85		24.50	34.96
Net NPA(per cent)	1.00	0.80	1.84		1.6	1.96		1.69	3.17
ROA	1.00	0.85	0.66		0.74	0.69		0.75	0.33
Cost Income Ratio	Reduce 2 per cent p.a till 40 per cent	46	43.51		43	42.24		41.00	39.33
Union Bank of India									
Adv. To Weaker Sections	10	10	10.12		10	6.59		7.46	9.18
Gross NPA (per cent)	Below 2	2.4	2.37		2.65	3.01		2.95	2.98
Cost to Income ratio	40	43	47.85		47	43.15		44	44.70

IDBI Bank										
CASA Deposits	Improve 5 per cent p.a till 30 per cent		21		24	24.10		27.50	25.12	
Priority Sector Adv.	40	40	30.44		33	31.51		37	22.30	
Direct Agri. Adv.	13.5	13.55	5.70		9.00	4.99		10	2.80	
Adv. To weaker sections	Improve 2 per cent p.a till 10 per cent	10.01	2.64		4	3.26		4	3.12	
ROA	Improve min by 0.20 per cent p.a till 1 per cent	0.70	0.73		0.80	0.81		0.9	0.69	
Central Bank of India										
ROA		0.8	0.8	0.70	1	0.55	0.26		0.55	0.44
Gross NPA (per cent)	Below 2	2	1.82		3.34	4.83		3.70	4.80	
Cost Income Ratio	Reduce 2 per cent p.a till 40 per cent	49	60.68		54.64	57.11		53	57.16	

(Source : Records of DFS)

The table indicates that the SOI targets were less stringent than the targets associated with the sanction orders. The table also indicates that the actual achievements were poor compared to the SOI targets. Thus, even the targets set in the sanction orders for 2010-11 were not actually achieved.

Audit did not find evidence that incorporation of the conditions set in the sanction orders was actually monitored by DFS. SOI, however, is reviewed regularly by the banks themselves as well as by DFS and as such, the SOI targets ought to have been set in line with the targets associated with infusion of additional capital.

In its reply (April 2017) DFS did not provide any justification for the mismatch between conditions in the sanctions and SOI targets.

4.2 Memorandum of Understanding

In February/ March 2012, DFS introduced the mechanism of Memorandum of Understanding (MoU) with PSBs to ensure that they lay down a firm plan for long term business development and performance enhancement and relate the same to their capital requirement. The MoU, signed by the PSB and DFS, consists

of a set of agreed targets that the PSB is expected to achieve which would form the basis for future capital infusion by GOI. The objective of the MoU was to achieve optimum utilization of scarce capital funds, with PSBs focusing on improving their efficiency simultaneously with the infusion of capital.

Audit noticed infirmities in preparation, finalisation and monitoring of MoUs. It was also noticed that MoUs had not been the basis for GOI capital infusion in PSBs during 2011-17.

4.2.1 Targets set for PSBs and efficiency

Audit noticed that the targets set against some of these parameters were decreasing, year-on-year, indicating that a lower efficiency was being targeted, as tabulated below :

Table 4.2: Targets set for PSBs and efficiency

Parameter	Targets vis-à-vis Achievements
CASA	For State Bank of India, the actual CASA was 48.66 per cent in 2010-11, whereas the year-wise target was set at a lower 45 per cent for all the years from 2011-12 to 2014-15. For United Bank of India, the CASA targets reduced progressively each year from 39 per cent in 2011-12 to 37 per cent in 2014-15
Cost to Income Ratio	For IDBI Bank Ltd, while the actual Cost to Income Ratio for 2010-11 was 35.15 per cent, the target for 2011-12 was pegged at 39.4 per cent indicating that the target set for future was lower than the current achievement. The targeted Cost to Income ratio was set at progressively higher rates in case of PNB over 2011-12 to 2014-15.

(Source : Records of DFS)

In its reply (April 2017) DFS did not comment on the reasons for setting lower targets for successive years.

4.2.2 No specific targets set for some parameters in the MoU

For certain PSBs (e.g., Andhra Bank and Allahabad Bank), specific targets were set for all components of RBI ratings. In case of other PSBs (e.g, Bank of Maharashtra, Bank of Baroda, Bank of India and Indian Bank) the targets were non-specific; - "shall improve upon existing rating on all parameters, particularly on Asset Quality, Management, Systems and Control".

4.2.3 Delay in fixing MoU targets

The MoUs were to be finalised by 30 November, 2011 as per directions of DFS. However, the MoUs were signed in February / March 2012, indicating a delay of nearly three months from the stipulated date. Further, the signed MoUs included targets to be achieved by 31 March, 2012. With MoUs signed as late as March 2012, the status of achievement on targets for 2011-12 were a foregone conclusion. In fact, the MoUs between SBI and its Associate Banks (State Bank of Bikaner & Jaipur, State Bank of Travancore, State Bank of Mysore, State Bank of Hyderabad and State Bank of Patiala) including targets for 2011-12, were signed in the 1st week of April 2012.

DFS replied (June 2017) that DFS had started discussions with the Banks immediately after the draft MoUs were sent to them and the numbers were indicated to them, so while signing might have been delayed the targets were known to them.

The reply of DFS has to be considered in light of the fact that only draft MoUs were circulated to all PSBs in October 2011, which were significantly different from the actual MoUs that were signed (February / March 2012).

4.2.4 Validity of MoU and targets fixed

The MoUs were to be valid for a period of five years. Audit observed that, with the exception of Central Bank (for which targets were fixed from 2012-13 to 2016-17), for all other PSBs, the signed MoUs contained targets to be achieved only till 31 March 2015. This indicated that targets were not fixed for the full period of MoU validity.

DFS replied (June 2017) that DFS entered into MoUs initially for period of three years and the targets were given till 2015, adding that all these targets were parts of the final targets and laid a roadmap towards achievement of the final or ultimate targets by 2017. DFS also replied that the targets given to the Banks to be achieved by 2015 were interim targets preparing the banks for achieving the ultimate or final target in 2017.

The reply of DFS was not acceptable on the following grounds;

- (i) The forwarding letters from DFS to the individual PSBs enclosing the signed MoUs, mentioned that the PSBs had signed MoUs wherein certain long term targets were to be achieved by the bank upto 31 March, 2015, with no reference to March 2017.
- (ii) The last column in the annexure to the signed MoUs contained targets to be achieved by FY 2014-15 only. These targets were not designated as 'interim targets' in the signed MoUs.

4.2.5 Mismatch between MoU and SOI targets

The targets for the years 2011-12 to 2014-15 were fixed in the MoUs which were signed in February/March 2012, while the SOI targets are fixed annually. Out of the 44 parameters under SOI, there were five parameters which were common with those in the MoU, [CASA, ROA, Cost to Income Ratio, Net Profit Per Employee (₹ in lakh) and Ratio of Staff in Branches to Total Staff]. **Annexures III to VI** contain a comparison between the targets in SOIs and MoUs across the five common parameters. Audit observed that there was significant variation between targets in SOIs and MoUs for the same parameter, with the maximum variation being the following:

Table 4.3 : Mismatch between MoU and SOI targets

Parameter	Maximum Difference
CASA (per cent)	18
ROA (per cent)	1.37
Cost to Income Ratio (per cent)	21.3
Net Profit per Employee (₹ in lakh)	10.15
Ratio of Staff in Branches to Total Staff (per cent)	10.23

(Source : Records of DFS)

DFS admitted (April 2017) that normally the targets for MoU and SOI should have been similar but due to changing assumptions, targets were not harmonized which should have been taken care of.

4.2.6 Progress reports on MoUs not monitored

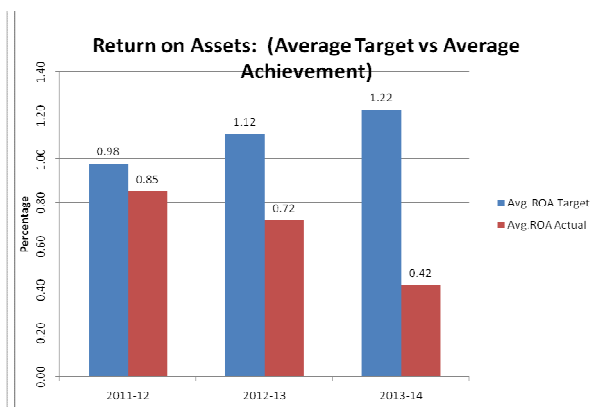
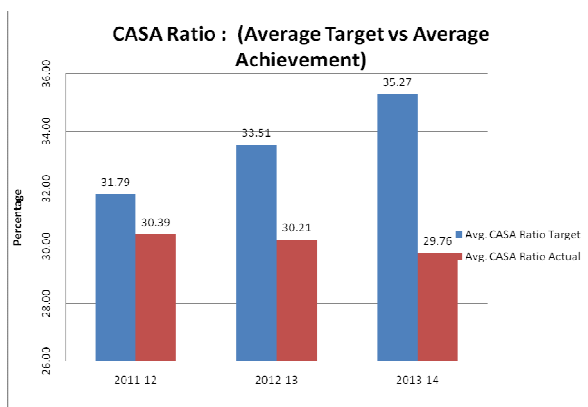
DFS had forwarded a copy of the signed MoUs to PSBs, stipulating that the bank would submit a progress report every quarter on the performance of the parameters stipulated in the said MoU. 273 progress reports were to be received from 21 PSBs (one from each PSB for Q4 of 2011-12, four from each PSB for each FY from 2012-13 to 2014-15). However, only 21 (for 4th Quarter of 2011-12 only) progress reports were received from PSBs indicating deficient monitoring of the performance of PSBs against agreed targets through progress reports.

In its reply (June 2017), DFS stated that the performance of the PSBs was done on a regular basis and DFS' senior officials have regular meetings with senior management of Banks to assess the performance of PSBs, with clarifications for non performance also sought and detailed structured study was undertaken by DFS for all PSBs on a quarterly basis. DFS also stated that the Finance Minister also did a review on a quarterly basis and GNDs as GOI representatives took active participation in the Board and also discussed the same with senior management of the PSBs. DFS further stated that they did not follow up for progress reports as they were able to monitor performance through the mechanisms mentioned above.

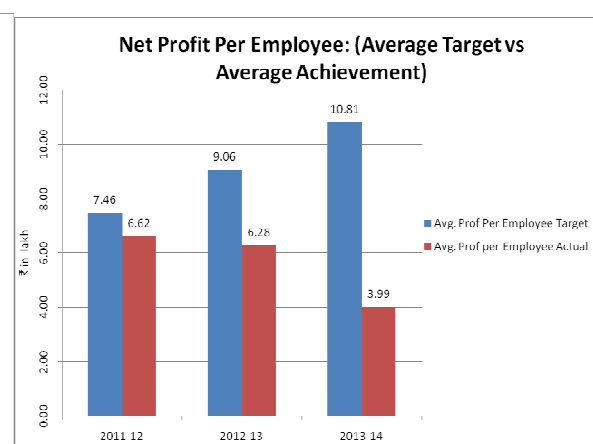
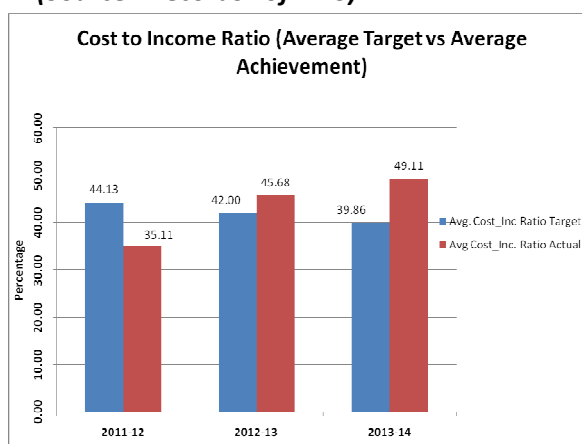
The fact remains that there was poor compliance by PSBs with regard to submission of quarterly progress reports. Further, there was no evidence to suggest that DFS had analyzed the achievement / non-achievement against targets in signed MoUs and linked the same to capital infusion.

4.2.7 Non-achievement of MoU targets

From records made available, Audit observed that there was under-achievement of targets, in respect of the five parameters [CASA, ROA, Cost to Income Ratio, Net Profit Per Employee (₹ in lakh) and Ratio of Staff in Branches to Total Staff] for the FY 2011-12 to 2013-14, as shown in **Annexures VII to IX**. The charts on the next page show the under-achievement in targets during 2011-12 to 2013-14, measured through the average value of four parameters [CASA, ROA, Cost to Income Ratio, Net Profit per Employee (₹ in lakh)] for PSBs:



(Source : Records of DFS)



(Source : Records of DFS)

The widening gap between targets in MoUs and achievements with every passing year is an indication that the performance of the PSBs was not in sync with the targets.

In its reply (April 2017), DFS stated that the performance of all PSBs was analyzed at DFS on a quarterly basis on various parameters including those included in MoU and was discussed with individual banks at the highest level.

The fact remains that the targets stipulated in the signed MoUs were not achieved.