

## RBI welcomes bank recapitalization plan

A well-capitalized banking, and in general, financial intermediation, system is a pre-requisite for stable economic growth. Economic history has shown us repeatedly that it is only healthy banks that lend to healthy firms and borrowers, creating a virtuous cycle of investment and job creation. The Government of India's decisive package to restore the health of the Indian banking system is in the view of the Reserve Bank of India (RBI), a monumental step forward in safeguarding the country's economic future. For the first time in last decade, we now have a real chance that all the policy pieces of the jigsaw puzzle will be in place for a comprehensive and coherent, rather than piece-meal, strategy to address the banking sector challenges. It bodes us well that this step has been taken in a time of sound macroeconomic conditions for the economy on other fronts.

The proposed recapitalisation package for the banking sector combines several desirable features. First, by deploying recapitalisation bonds, it will front-load capital injections while staggering the attendant fiscal implications over a period of time. As such, the recapitalisation bonds will be liquidity neutral for the government except for the interest expense that will contribute to the annual fiscal deficit numbers. Second, it will involve participation of private shareholders of public sector banks by requiring that parts of the capital needs be met by market funding. Last but not the least, it will allow for a calibrated approach whereby banks that have better addressed their balance-sheet issues and are in a position to use fresh capital injection for immediate credit creation can be given priority while others shape up to be in a similar position. This provides for a good way of bringing some market discipline into a public recapitalisation program compared to the past recapitalisation programs.

Financial sector policies should support growth while maintaining financial stability. On behalf of the Reserve Bank of India, I commend the government on its bold steps in this direction, starting with implementation of the Insolvency and Bankruptcy Code that is helping resolve the underlying corporate stress, and culminating in yesterday's announcement of the public sector bank recapitalisation program. The RBI looks forward to working with the Government to ensuring these plans reach their natural completion to the benefit of the broader Indian economy.

(Urjit R. Patel)  
Governor