FIBAC 2016

BANKING HORIZON: CLOUDS & SILVER LININGS

S. S. Mundra
Deputy Governor
<table>
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<tr>
<th>GLOBAL SKYLINE</th>
<th>EVER-CHANGING CONTOURS</th>
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<td>• Brexit (End or beginning?)</td>
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<td>• US Rate Action</td>
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<td>• Volatile Chinese Growth</td>
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<td>• Euro Zone Banking System</td>
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<td>• Hesitant Economic Recovery</td>
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<td>• Ultra Accommodative Monetary Policies</td>
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<td>• Negative Rate Of Interest</td>
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**Will these bring rains or storm?**
REGULATION

• Regulation – More intrusive
  ▪ A daunting New Vocabulary (TLAC, CCB, LCR/ NSFR, SIFIs, Volcker Rule/ Living will & so on)
  ▪ Risk weight for Sovereign Assets?
  ▪ New standardized approach for Credit risk?
  ▪ Penalties
  ▪ Stress test – Capital
  ▪ Nearer Home – IFRS

• Impact on Banks profitability

  Do regulators need to worry about that?

ASSET QUALITY REVIEW
STILL A WORK-IN-PROGRESS

- Stressed Assets
- Agenda for remaining 3Q of 2016-17
  - Provisioning need – Fresh & incremental – profitability impact
  - Crystallization of Non-Funded Exposures
  - Sitting stunned is no solution – Use tools judiciously – Overblown fears – Resolution can’t be delegated
  - “Small Tickets” don’t translate into “Small Attention”
  - Credit Migration – Cherry Picking
CREDIT

Churn in Credit Market

- Corporates – Reality check

- Corporate Leverage
  Of a sample of 3,700 listed non-financial companies*
  - 37% had interest coverage (IC) < 1
  - 32% were chronically stressed (having IC < 1 for four or more of the past eight quarters)
  - Many of them face refinancing risk in coming years**

At the same time – Review of Exposure limit – Move to market Opportunity to rebalance portfolio

- Estimated 78% MSME source credit – self/informal channels. Riskier standalone – However, more diversified at portfolio level than large corporates

- Rising middle class/ Urbanization – Retail opportunities – However, caution against – adverse selection/over lending – Need for accredited Credit Counselors

- Agriculture – Risk without enhanced credit absorption capacity – Land reforms – Investment – Technology – Insurance

* Source: Credit Suisse ** India Rating Research
COMPETITION

- New Institutions: Banks – SFB, PB
- New Competitors: Non-bank actors - P2P, Crowd-funding, PPI, TReDS
- Joint origination – Banks/NBFCs/MFIs – Merits a look
- New Customer & New Channels – Fintech
  - How are you preparing for the future – and it is not too distant
- **Customer Service - No more lip service**
  - Mis-selling – Establish suitability
  - Institutional might v/s individual fragility
  - Account No. Portability- No longer a remote possibility – UPI – a game changer
  - Account opening – Pleasure or Pain

OPERATIONAL

- **Cyber Security- Bane of technology**
  - Hits and near-misses

- **Frauds- History continues to repeat itself**
  - Import Remittance Scam, Fixed Deposit Frauds, LCs, Bill-discounting, BGs

- **KYC/AML**
  - Decline in Correspondent Banking arrangements
  - Life after PMJDY – Too many ring masters
  - Return on efforts & resources (Business model still evolving)
  - Promoting usage, Preventing misusage (Money Muling)
  - Ecosystem (Branch – BC balance)

- **Strong Central – processing and surveillance – 3 lines of defense – ignore at your peril**
BEYOND THE CURB

• Technology – a big enabler – a potent risk

• Digital payments – Digital currency – Distributed Ledger – Cloud Computing – and so on

• Journey – Big Data – Analytics – AI – Robotics
  (Level of understanding and preparedness)

• Regulatory stance – still evolving – However as MAS puts it “Materiality & Proportionality” “Regulatory Sandbox”

• Back office technology sharing (HSBC | Morgan Stanley) – represents significant % of operating cost
THE LAST WORD

• “Finance exists to serve the real economy & society too. It is means to an end & not an end itself”
Reasons to become concerned if it overtakes Real Economy or Trading & fee generation becomes more important than lending

• G-30 Report – “The Board & the senior management need to make sure that the voices of the middle management & the echo from the bottom can be heard”
Silver linings are not elsewhere... They are at the edge of clouds only.

Thank you.