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MISSION

The mission of the Institute is to develop professionally qualified and competent bankers and finance professionals primarily through a process of education, training, examination, consultancy / counselling and continuing professional development programs.

ध्येय

संस्थान का ध्येय मूलत: शिक्षण, प्रशिक्षण, परीक्षा, परामर्शिता और निरंतर विशेषज्ञता को बढाने वाले कार्यक्रमों के द्वारा सुयोग्य और सक्षम बैंकरों तथा वित्त विशेषज्ञों को विकसित करना है ।

Printed by Shri J. N. Misra, **published by** J. N. Misra on behalf of Indian Institute of Banking & Finance, and **printed at** Onlooker Press 16, Sasoon Dock, Colaba, Mumbai-400 005. and **published from** Indian Institute of Banking & Finance, Kohinoor City, Commercial-II, Tower-I, 2nd Floor, Kirol Road, Kurla (W), Mumbai - 400 070. **Editor** Shri J. N. Misra.

Dr. J. N. Misra
Chief Executive Officer, IIBF, Mumbai

The Asia Pacific Association of Banking Institutes (APABI) is an informal association of Banking Institutes of Asia-Pacific region. Currently, there are 18 member Institutes in APABI. The APABI conference, along with its executive meeting, is organised by one of the APABI member institutes on a rotation basis, for a period of 2 years. IIBF was the host Institute for APABI meeting & conference for the period 2013-15. The institute had organised the APABI International Conference-2014 in Mumbai on the theme "Talent Management in Banks". This was followed by APABI conference 2015, on the theme "New Paradigms in Banking" in New Delhi on 23rd September 2015.

This issue of Bank Quest contains the report of the recent Conference in New Delhi.

The first article contains the Welcome Speech by the CEO of IIBF elaborating the theme and the topics to be discussed in the conference.

The second article is the address by Mr. Ashwani Kumar, CMD, Dena Bank and President of the Institute. He emphasized the importance of the theme of the conference & appreciated the relevance of the conference in today's context.

The third article is the special address given by Mrs. V R Iyer, Member (Finance &Investment), IRDAI.

The Conference was designed with an inaugural session followed by three consecutive panel discussions. The topics discussed in these three panel discussions were "New Paradigms in Banking", "Inclusive Banking Experiences" and "Payment Systems: Evolving Paradigms" respectively. The topics for each panel discussion were chosen with care after considering its contemporariness and its importance in today's context.

The first theme presentation & the details of the panel discussion on "New Paradigms in Banking" is covered as the fourth article.

The second theme presentation by Mr. S. Muralidaran, Director (Academics), IIBF on "Inclusive Banking Experiences" and details of the panel discussion is covered as the fifth article.

The sixth article contains the theme presentation on "Payment Systems – Evolving Paradigms" by Mr. S. K. Datta, Joint Director, IIBF and the panel discussion on the topic.

The seventh article is on various Learnings from the Conference.

On conclusion of the APABI Conference, the 32nd Sir Purushotamdas Thakurdas Memorial Lecture was held. The speaker on the occasion was Mr. Chris Harvey, Managing Director & Global Leader of Financial Services, Deloitte, Hongkong. Mr. Harvey spoke on 'The Future of Financial Services: How Disruptive Innovations are Reshaping the way Financial Services are Structured, Provisioned and Consumed'. His speech is covered as the eighth article.

We also carry a book review by Mr. Avinash Chander Mahajan, Chairman, Banking Codes & Standards Board of India, on 'Smart Manager – Retail Banking Decoded', a book written by Ms. Poppy Sharma, Chief Manager (Faculty), Central Bank of India.

We welcome readers' suggestions and feedback for improvement.

Dr. J. N. Misra

Welcome Speech

Dr. J. N. Misra*

It is a great honour for IIBF to host the Asia Pacific Association of Banking Institute's (APABI) International Conference-2015 in New Delhi.

We have with us Mr. Ashwani Kumar, CMD, Dena Bank and Vice President of IIBF to preside over this inaugural session and deliver the president's address. I welcome you Sir and request you to Preside over the session.

The Governing Council of IIBF had constituted a Steering Committee for guiding the Institute to organise this Conference. Mrs. V.R. Iyer former CMD of Bank of India and currently, Member (Finance & Investment), IRDAI spearheaded the Committee and had guided the Institute. Today, in this inaugural session, Mrs. V.R. Iyer is with us to give her special address. I heartily welcome you Madam to this Conference.

I also welcome Mr. Chris Harvey, Managing Director & Global Industry Leader of Financial Services, Deloitte, Hong Kong, who will be delivering the 32nd Sir Purshotamdas Thakurdas Memorial Lecture this evening.

For this Conference, we have invited many of our fellow institutes in Africa and Middle East in addition to the APABI members.

The Asia Pacific Association of Banking Institute's (APABI) is an informal association of Banking Institutes of Asia-Pacific region. Currently, there are 18 member Institutes in APABI. The APABI conference along with its executive meeting is organised by one of the APABI member institutes on a rotation basis. The Institute, for holding APABI and the Chairmanship of APABI for a period of 2 years, is decided in the APABI meeting. During the 2-years period, the member institute holding the Chairmanship hosts the APABI Meetings and Banking Conferences once a year. IIBF had organised the APABI International Conference-2014 in Mumbai on the theme "Talent Management in Banks" and it was well attended by bankers and international delegates.

I am happy that IIBF is hosting the APABI conference 2015, on the theme "New Paradigms in Banking". Considering the rapid transformations being witnessed in the banking and finance space, the APABI Steering Committee headed by Mrs. V.R. Iyer aptly chose the theme for this International Conference.

The Conference is designed with an inaugural session followed by three consecutive panel sessions. Each panel discussion will commence with a brief theme presentation and will set the floor for the panel discussion. For the purpose of this Conference, the Institute had asked feedback on issues related to the theme of the session from banks in India. The theme presentation also includes the summary of feedback received from banks. After the brief theme presentation, the Chairman of the session will initiate the discussion with his panel members by raising the issues concerned on the topic. The panel may also share their views on a few questions from the participants. At the end, the Chairman will give his concluding remarks.

The topics to be discussed in these three sessions are "New Paradigms in Banking", "Inclusive Banking Experiences" and "Payment Systems: Evolving Paradigms" respectively. The topics for each panel discussion were chosen with care after considering its contemporariness and its importance in today's context.

Banking of yore is completely different from banking as of today and banking in future will be different from how banking is being performed now. This has happened due to the paradigm shifts which have been witnessed.

*** Chief Executive Officer, IIBF**

Inclusive Banking is on a mission critical mode. The second panel will therefore, discuss myriad issues on the subject and the way forward. The third panel will deliberate on the changes, which have happened in the payments space, growth in digital payments, challenges being faced by banks and the opportunities available to different institutions.

The APABI Conference-2015 will be followed by the 32nd Sir Purshotamdas Thakurdas Memorial Lecture. The topic of the Lecture which is "The Future of Financial Services: How disruptive innovations are reshaping the way financial services are structured, provisioned and consumed" is in tune with the theme of the Conference.

I hope you will discuss, share and enjoy this Conference. I now request Mr. Ashwani Kumar, CMD, Dena Bank and Vice President of IIBF to share his views and welcome the Chief Guest to inaugurate the Conference.

Recent regulatory initiatives on asset quality

The Reserve Bank has taken a number of regulatory initiatives to further strengthen the credit risk management at banks, like withdrawal of the special asset classification benefit on restructuring of advances with effect from April 1, 2015, increasing the quantum of provisioning on 'standard' restructured assets to 5 per cent and enhancing promoters' contribution to restructured assets. These measures are in line with the international best practices and were meant to dis-incentivise ever greening of loans in the guise of restructuring.

A comprehensive framework for revitalising distressed assets in the economy was initiated in January 2014 which outlined setting up a Central Repository of Information on Large Credits (CRILC) to collect, store, and disseminate credit data to lenders. Other measures included setting up of Joint Lenders' Forum (JLF), early identification of problem accounts by banks, timely restructuring of accounts which are considered to be viable, and encouraging banks to take prompt action for recovery of loans. The concept of non-cooperative borrowers was also introduced, providing for higher provisioning norms for such borrowers. In order to ensure high level of representation from banks in JLFs and approval of Corrective Action Plans (CAPs) by a high level body having impartial views, Reserve Bank has recently introduced JLF-Empowered Groups (JLF-EG), constituting Executive Director level representations from top lending and non-lending banks to the specific borrower under a JLF.

The Reserve Bank's strategic debt restructuring (SDR) scheme provides that the lenders under the JLF have the option to convert their existing loans into equity under a revised pricing formula of the Securities and Exchange Board of India (SEBI) in order to collectively become majority shareholders of a borrower company which fails to meet the milestones set up under a restructuring package. This pricing formula minimises the conversion loss to banks, which are also given moderate asset classification benefit for 18 months. In order to provide flexibility to banks' in effecting a change in ownership of borrowing entities, which are under stress primarily due to operational/ managerial inefficiencies despite substantial sacrifices made by the lending banks, the Reserve Bank has allowed banks to upgrade the credit facilities extended to borrowing entities whose ownership has been changed outside SDR (for instance by invocation of pledge and subsequent sale of shares, issue of new shares to a new promoter and acquisition of the borrower company by a new promoter), to 'standard' category upon such change in ownership subject to certain conditions.

Source : Financial Stability Report, Issue No. 12, Reserve Bank India, December 2015

President's Address

Ashwani Kumar*

It is my privilege to welcome you all to the Asia Pacific Association of Banking Institute's (APABI) International Conference in Delhi, the capital city of India. APABI Conference is an important event organised by one of the APABI Member institutes on rotation basis. In the past, these conferences have been found to be useful for member Institutes of APABI and their member banks. IIBF had organised the APABI International Conference-2014 in Mumbai and more than 200 delegates including 40 international delegates had attended the Conference. I am happy that IIBF is organising the APABI conference 2015 in New Delhi. For this Conference, the Institute has invited many of our fellow institutes in Africa and Middle East in addition to APABI members. I welcome you all to this Conference. I learnt that representatives of APABI and non-APABI countries met yesterday and deliberated on what all could be done together in capacity building, in the banking & finance sector.

This year's Conference on the theme "New Paradigms in Banking" is aptly chosen to provide an opportunity to learn, share experiences and best practices due to the evolving paradigm shifts in banking operations particularly in a globalised banking environment. Dr. J.N. Misra, Chief Executive Officer, IIBF has already provided a brief outline of the theme and the sessions of the Conference. In brief, the Conference is designed in three sessions viz. New Paradigms in Banking, Inclusive Banking Experiences and Payment Systems: Evolving Paradigms. I am sure all the delegates could look forward for interesting and fruitful deliberations throughout this full day conference.

We have seen that globalization has transformed the banking landscape by changing the traditional business models. Further, the global crisis-2008 has led to sharp refinement of supervisory and regulatory norms in the form of BASEL-III. Simultaneously, banking sector is witnessing changes in customer preferences and increased expectations. Due to these changes, banks had to make shifts in systems, processes, strategies and evolve newer products/ services mainly technology driven products on a continuous basis. In order that they stay ahead in the business, banks are also striving to improve their performance from time to time. The emerging focus areas are risk management, compliance, IT, business analytics, financial inclusion etc. With the banking sector becoming increasingly complex, competitive and customer oriented, banks have started exploring and experimenting newer business models to meet the increasing challenges not only in India but also in the Asia Pacific region.

We have been involved in financial inclusion for a long time. In the areas of financial inclusion, we have made many achievements. However, there is still a long distance to traverse. The Government is providing a lot of emphasis on financial inclusion and the Pradhan Mantri Jan Dhan Yojana (PMJDY) has been launched during the last year to achieve comprehensive financial inclusion. In order to achieve this, currently multiple models like SHG-Bank Linkage, MFI lending, BC models etc. are operating. We have opened many accounts under PMJDY. Many of these accounts are dormant and transactions are not happening. If transactions happen in these accounts, then only the purpose of opening of the accounts will be served. How do we increase transactions in these accounts? The ICT driven BC model has several challenges. The capacity building of BCAs is an important issue. There are many players in this field. How do we synergise the efforts of different stakeholders? In this Conference, we have participants from Asia Pacific, Africa and Middle East countries. I am sure that there are lessons to be learnt from these countries. It will be a rewarding experience.

The changes in the payments industry are driven by innovations across industries such as retail, telecom,

* Chairman and Managing Director, Dena Bank

banking and financial services combined with changes in the way in which consumers communicate and make purchases. Today, consumers can purchase goods and services using cards, cheques, PayPal, and increasingly, through use of social media and mobile phones. The growing ease and convenience of new and emerging payment systems allowing anytime, anywhere payments is tempting to both consumers and the merchants' ecosystem. The industry is exploring to identify the ideal payment instrument, which would have characteristics of:

(1) Universality – everyone should be able to use it for all types of payments

(2) Convenience – easy to use, cheap and always available

(3) Security – people need to feel safe using it

(4) Certainty of Value – it needs to be as good as cash for transfer of value with a clearly defined repudiation / non-repudiation mechanism.

Let me raise some of the issues confronting today's Banking Industry in certain areas so as to discuss and explore solutions in this Conference.

Regulatory changes are forcing the banks to change the way they are doing business these days. Banks need to comply with the guidelines of BASEL-III.

On the one hand, banks are facing increasing stressed assets and on the other hand, a large number of people are still outside the purview of formal banking channels.

Digital Banking is the pivot around which banking is expected to revolve in future. In order to make it a success, banks need to redeploy resources, including capital, people and technology, redefine the boundaries of their operating models to address customer expectations proactively. Each bank will have its own journey and the success lies in executing the right model at the right speed.

Many new banks are entering. Small Banks/Payment Banks are expected to give competition to the existing banks.

- In these days, banks are able to capture a large amount of data on account of technology. In order to remain competitive, banks will need to extensively use data mining / data analytics for improving customer retention and for increasing business volumes. There are impediments which banks are facing in using these tools such as data residing in too many divisions, time involved in analysis, lack of availability of skilled personnel for analysis, cost involved etc. How are banks going to resolve these issues?
- With the use of technology in banking, no doubt customer convenience in terms of efficiency has increased. But at the same time, potential threat of cyber-crimes and fraud also is on an increasing trend. Additional safeguards will be the need of the day.
- Coming to inclusive banking, many steps are being taken from the supply side. There is an urgent need to attend to the demand side barriers. Though measures are being taken to extend financial education & literacy to the masses, we are yet to see tangible results in a sustainable way.
- JAM - Jan Dhan, Aadhaar and Mobile is the new mantra for future payments. There is a need to make the Payment Systems more cost effective and sustainable.

I have shared some of my perspectives on the theme and raised some of the issues confronting banks. I hope the Conference will discuss and deliberate on some of these issues.

With this, I wish a thought-provoking Conference and now, I request Mrs. V. R. Iyer to inaugurate the Conference and deliver her keynote address.

Special Address

Mrs. V R Iyer*

IIBF has been doing an excellent service in the field of education and training, as depicted in the short film shown earlier. I too was associated with IIBF activities when I was in the banking sphere for decades.

Let me start by complementing the Indian Institute of Banking and Finance for selecting the main theme - Changing Paradigms in Banking, which is very topical and relevant for all the bankers today. By organising this discussion on the eve of the APABI Conference, it will further spur thoughts and debates in these areas. That this discussion has drawn doyens from the financial industry is a testimony to the importance of the subject matter that we face as a banking community.

It is my pleasure to be here amidst all of you.

Last 7-8 years has been eventful, interesting and also challenging, especially for the policy makers across economies. Crisis after crisis in fact have tested the existing policies, forced re-orientation of many of the policies being followed and led to the adoption of new and unconventional policies. In fact, the intensity of the last global financial crisis of 2007-08, has been such that financial landscape has undergone tectonic shifts. Against this background, I would like to touch upon briefly the global outcomes and the impact of such changes and then briefly touch upon changes that is taking place in the landscape of Indian Banking and the banking industry in general and of the imperatives for the banking community.

If you really introspect what causes a paradigm change, I feel there are four causes that result in a paradigm change:

- Macro-economic crisis
- The technological advancement that takes place from time to time
- Revolutionary product development and the changes in the banking environment and
- The regulatory changes that take place from time to time

I will now set out my thoughts on how some of these issues are influencing the banking industry. It is my expectation that the forces of the ecosystem are going to compel the bank management to deconstruct their business models, take a hard look at the value proposition and reconstruct the value enriching models.

Financial crisis as a phenomenon has been recurring at frequent intervals. Every crisis is new, but the impact of it is more or less similar. The major crisis faced by the banking industry in the recent past are the Asian Financial Crisis in 1997, Long Term Capital Management (LTCM) and Russian Default in 1998, dot-com crisis in 2000, Subprime crisis in 2007-08, the European Sovereign Debt Crisis in 2011, the Fed Reserve Tapering in 2013 also caused much volatilities for the rest of the economies and the recent Eurozone and Greek Crisis.

The crisis of 2007-08 is considered as the mother of all crisis, which warranted substantial pumping in of liquidity to bail out the entire financial system. Most of the economies are still reeling under the adverse impact of the crisis. Even the developed economies are yet not out of the woods and global recoveries continue to be very weak. Crisis has only indicated that much of the damage is self-inflicted, the result of greed, fraud, poor management or poor corporate governance. We are witnessing a new world order during the last 5-6 years. Higher levels of regulatory oversight has come to play, which is understandable given the large amount of tax payer's money that has gone to support the financial system.

The IMF has projected the global growth at around 3 % lower than what was projected in the world economic outlook in Oct 2014. The revision reflects a reassessment of the growth prospects in China, Russia, Eurozone, and Japan and some of the exporting countries. World trade volumes have been declining year after year. So also the consumer prices.

*** Member (Finance & Investment) Insurance Regulatory and Development Authority of India**

Japan can come out of the technical recession this year, but still, they have quite some distance to go through. Bank of Canada and Reserve Bank of Australia have announced rate cuts in view of weak growth. Eurozone, of course, continues to be a matter of concern, as also Greece, which has recently received a bailout plan. Ukraine and Middle East are sources of geopolitical risk. Overall growth continues to be in a sluggish phase for all of us, across the world. Most of the countries are finding it difficult to increase the rates of interest. Even the US has again, in view of the market volatility, decided to continue with a near zero percent ROI as of now and has put off any rise in the ROI for some time to come (maybe 2-3 months).

As banking mirrors the economy, banks in the developed economies too have been slow to heal from the crisis. Besides, the aging population and the low productivity there have sapped the ability of advanced economies to a greater extent to sustain the higher rates. All this has led the banks and FIs in revising down their expectations for revenues and earnings. Other factors though are in play. Most important is the enhanced regulation, which we are all witnessing and super visioning brought out by the crisis. It has prompted banks to exit some activities completely and alter their balance sheet. Capital adequacy prescription by BASEL at one stroke has changed the banking scenario very dramatically - pulling down the energies like the gravitational force pulling down an alien while landing on earth. After all capital adequacy is nothing but a novice depositor's question to the bank "what is your debt equity ratio", before giving his deposit.

If you look at the changes in the BASEL regime, the levels in the quality of equity capital and liquidity have soared very high. The capital and liquidity requirement in India will come into full force by March 2019, and Jan 2019, respectively.

Bank boards and senior managements across the countries are being held to account for the consequences of their actions or their inactions. A related and apparently inevitable consequence of all the regulatory changes put in place is that the bank's return on equity will be lower than pre-crisis. This is especially because of the magnitude and the volume of capital that is required to be pumped into the banking system. In India alone, the amount is estimated to be almost ₹1 lakh crore, which has to be tapped from the capital market account. Besides, significant investments also need to be made and are being made in the IT infrastructure, data management and analytics to comply with the regulatory demands of the various management information systems and analytics.

Certainly, regulation has become a strategic risk, a strategic consideration for the banks, as supervisors are increasingly evaluating the business strategies and models of individual banks. Bank management will have to constantly evaluate where the revenues reside, where the cost can be contained, how to increase the spread and how can the return for the shareholders, for all the stake holders, be maximised.

Certainly, this calls for an overhaul in our thinking process in terms of models, in terms of pricing, in terms of reallocation of capital across different activators and focussing on efficiency of operation, profitability of the activators, supervision and control. Therefore, the regulatory compliance today has significantly increased for all of us. If you look at the domestic economy, of India's score card, what we are witnessing is only a slow economic recovery. As per the World Bank estimates - growth in 2015-16 may be around 6% or slightly lower also. The economic recovery in India is being helped by a decline in the inflation largely due to the weakening of global prices and also the commodity prices, which is coming handy to banks of our country.

Indian financial sector has traditionally been bank based. The banking sector has played a very significant role in the economic development of the country. The assets of the banking sector have increased manifold - almost 13 times from 1980. It has increased from 7.5 trillion to almost 98 trillion today. The non- food credit has expanded almost 17 times from 3 trillion to almost 53 trillion today. The credit to GDP ratio which was only 5% stands at around 56% today. SLR has already been declining almost from 38.5% to 22% now. All the while, the banking system has been robust in our country meeting all the potential standards.

During the recent financial crisis, and also due to the slowdown in the global and domestic economy, the Indian Banking Sector did prove largely resilient but it has also had its own share of adverse impact. We are witnessing issues such as lower growth, adverse impact on the asset quality, lower profitability, etc. Simultaneously, what we are witnessing in India is a change in the banking structure. All of you will be keen to debate on the emerging new banks. Two new banks will be coming into play, one has already come and one will come very shortly. RBI has announced in principle approval for 11 payment banks, which will come into play in the next 18 months or so. RBI has also given in principle approval for almost 10 small banks. The regulator is also keen to bring the licences for the new banks on tap. All these would lead to a new banking landscape during our lifetime itself. The inevitable story of the changing banking landscape would be that there would be more players in the industry. This would definitely threaten the position of the existing players at least in the medium term. Immediately one may not feel so, but not planning for that implies that in the medium term, we will lose out our market share.

Besides, with every major telecom player coming into the payment space now, the dominance of the banking structure in the payment system also would reduce gradually - unless the existing players innovate in their offerings and connect with their customers and staff members equally, because ultimately it is the staff who has to deliver. More players of course, it can be debated and argued, are required in our country because we have a vast majority of excluded population from the banking system.

With the strategic role of the Government of India (GOI), RBI and all the banking system, we have done a commendable progress in the financial inclusion space. Going forward, the challenge would be to find a financially viable solution for it. I personally feel that the sustainable growth in this space would call for the rural infrastructure development and also the stimulation of the rural economy for a livelihood generation. Of course, the Government is seized of it and they are engaged in finding ways to go about it.

In the current institutional landscape, I personally feel that NABARD can play a very definitive role here with new product offerings and new business models. Despite all these challenges, the net interest margin of banks has not suffered much. So it is said that Indian banking can face still more competition.

The key for banks going forward is of course cost containment, revenue maximisation by improving productivity and also increasing the third party/ fee income. It is also worth mentioning that we are already witnessing a change in culture of the corporate customers, who are already accessing the wholesale markets directly. The regulator is also keen that infrastructure and project finance should get financed by the equity market and the bond market. All this calls for innovations to meet the expectations of the retail customers in their transaction banking and also in the business of the SME customers, who are more loyal and where the yields are high. All that the SMEs' desire is good relationship management, fast credit decisions, and the complete product range at one stroke. The most important challenge for the bankers in India is how to meet the needs of the different segments of economy - in rural, urban and semi-urban centres. Of course, this needs to get powered by the IT systems, Data Management, and also analytical capabilities.

Coming to the field of technology, Information Technology and Electronic Fund Transfers have emerged as the twin pillars of the modern banking development. Products offered by the banks have moved beyond the conventional banking, no doubt in the last 5-8 years and access to these services have become around the clock. This indeed, is an evolution in banking. But we also need to recognise and acknowledge that - the new paradigms in payment systems which is taking place at a break neck speed. The last 10 years has seen a major shift in India from cash based systems to electronic payment systems, thanks to the various measures initiated including the introduction of the Payment and Settlement Systems Act, setting up of the robust RTGS and NEFT platforms, regulation and promotion of alternate channels and payment gateways and guidelines to the security measures that have been put in place.

What has incredibly influenced the payment system domain has been the development in the mobile banking space. Near field communication is also becoming a game changer in the reliable cashless payment system. Many of the PSBs and private banks actually have made an initial entry into this space. Momentum of course, is yet to pick up. In the non-banking space, Starbucks along with a number of retailers have in fact introduced new payment options through mobile apps, powered by near field communication systems. In the last two years, the number of mobile banking device used by customers has tripled and the cumulative value of the banking transactions have gone up 11 times. But the potential for mobile banking is still very large, still untapped and is available for all the existing players. There are over 900 million mobile users in the country. But there are only 36 million mobile banking customers. This will definitely get a fillip with the PMJDY schemes when it gets fully implemented.

A recent article revealed that mobile banking costs only 2% of the branch banking, 10% of ATM and 50% of internet banking. PoS is one area in fact that has spurred a revolution in digital transactions. It has seen innovations like mobile PoS, working in GPRS. In fact, it is going to be major player in India going forward in the e commerce segment. The latest development is to convert a mobile device, an iPad or a tablet into a bank.

Some of the banks have already gone ahead with that. Platforms like IMPS and other enabled payment systems are measures in the right direction. These will integrate the payment systems of the various G2P – Govt. to Public Transactions, and also enable the mobile phone to be used in a larger way. Mobile banking has a great future in India. In fact, M-cash or E-cash will replace the physical cash to a very large extent going forward. It is necessary that we become alive to the situation and start promoting products in this area. We are already witnessing from the youngsters that they feel it is not in fashion or they don't have time at their disposal, to make a visit to the bank, wait in the queue, fill up the forms and follow up all the processes.

We have seen complete transformation of the music and media industry with the advent of the digital era. Iconic technology companies like Google, Apple and Amazon with their technological and operational excellence have provided customers with unparalleled digital experiences. Non-banking challengers like Apple Pay in US, Alibaba in China, etc., are redefining the delivery of financial services. The line between the services offered by banks and non-banks will increasingly become blurred. In fact, the Central Bank of Brazil and the Financial Services Regulator in Peru have already issued regulations that allow the creation of a new entity for money issues under their licence. RBI, as an initial and a step forward have come out with payment banks and small banks and going forward, we can expect RBI to come out with opening up of the financial space in a still broader manner.

The customer will always choose the channel and we should be there to deliver in the days to come. Bank will have to become customer centric. Challenges towards this on the staff front will have to be addressed. It is my personal belief that banks in India should find ways to reinvent themselves in this new paradigm. With the rapid growth of mobile usage in the country, combined with the advancement of technology and also the facilitator regulation from the regulator, there is a tremendous opportunity for all of us to reach out, introduce new products, deepen customer relationship in the process, also contain the cost and most importantly, move forward in digitalising the economy.

Amidst the changing business environment, I would like to flag some issues for discussion:

1. Bringing down the barriers to entry in the banking industry - are we geared for a more competitive banking that is likely to emerge?
2. A paradigm shift is taking place in the global banking activity and its regulation with greater emphasis on managing financial risk. Are we adopting the right measures, the required and appropriate risk management practices, acceptable to the global norms and standards?
3. The technology change is affecting the banks as well as other industries. It can pose a threat as well as it can throw opportunities for all of us. The key point is, are we doing enough to leverage technology to our advantage? In the process, how are we empowering our staff members?
4. In view of the continued slow down, bankers have issues on asset quality concerns. Are we making efforts to look into our systems and making efforts to improve the credit appraisal at the origination and monitoring?
5. With advancement in technology and consequent increase in competitiveness and information, how are banks gearing to improve customer service? Customer service should be foremost, the fulcrum of whatever we are doing and are we able to offer a menu of choices to the customers? Also honing up the skills of the staff to manage the change is important.

In conclusion, recall Kodak, leader in cameras, who filed for bankruptcy in 2012, because the mobile phones have substituted the cameras today; Amazon's Kindle did the same to book retailers; Digital music has made CD-ROMs passé; WhatsApp has disrupted the telecom companies in their revenue model and Facebook has changed the way we connect with one another.

To borrow from Mr. Nandan Nilekani, "banking is having its WhatsApp moment now - it is for the bankers to warm up themselves to the idea". And to what Bill Gates said "banking will be required but banks may not be required to that extent."

This is already happening in developed economies and will catch up with the emerging economies like India. We should provide to customers, the entire range of financial services, which he/she wants anywhere and at any time. Customer centricity and agile infrastructure holds the key to build a bank for the future.

All of you will be deliberating today on the action that bankers need to take to prepare the banking sector to face the upcoming challenges. I am sure the panel discussions would throw many actionable points for all the banks.

☯

1st Session: New Paradigms in Banking

Theme presentation: Dr. J N Misra, CEO, IIBF

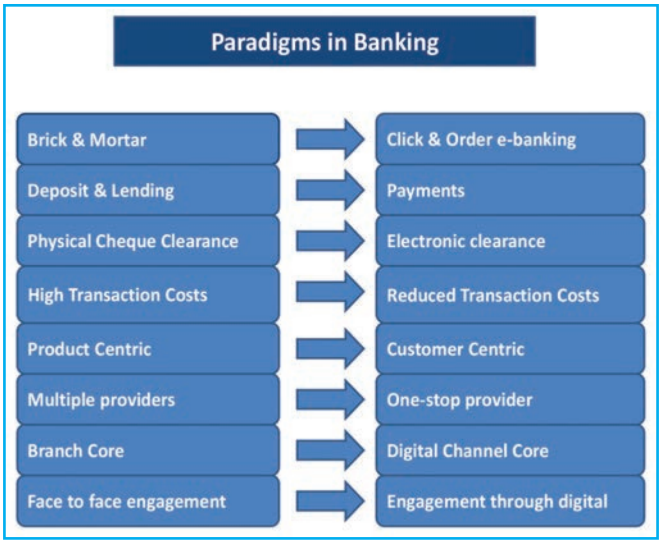
Panel: Chair: Arun Tiwari, CMD, Union Bank of India

Mr. Rajnish Kumar, MD (Compliance & Risk), State Bank of India

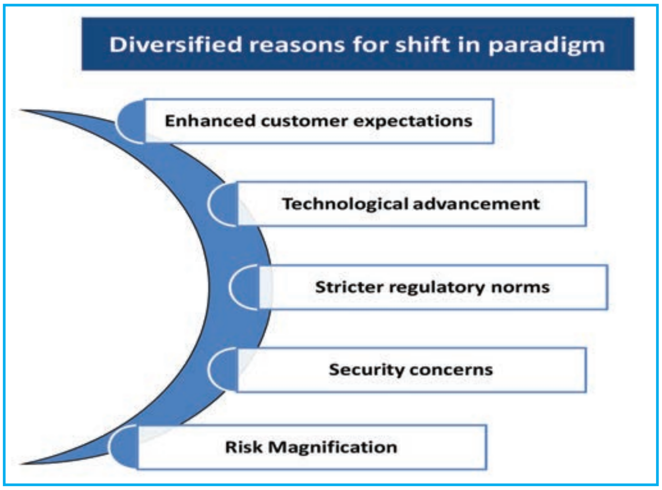
Mr. Saurabh Tripathi, Partner & Director, Boston Consulting Group

Mr. Tyrone Chen, Executive Vice President, Taiwan Academy of Banking & Finance

Dr. J. N. Misra introduced the panel members and elucidated that IIBF had sought the views of all banks on the theme under discussion. The feedback received from them was then incorporated in the presentations as discussion points for the distinguished panel for further deliberations.



Introducing the theme, Dr. Misra said that the changing face of banking is a reality. From brick and mortar to click and order banking, from deposit and lending to payments, from physical to electronic clearing, etc., the way banking is done has undergone a sea change. How we cope with the changing environment is the challenge before us. How we position ourselves with this change. It is essential that bankers are aware and prepared to handle the change.



The reasons for the shift in paradigm has been varied and has arisen on account of increasing customer expectation, fillip provided by technological advancements, the delivery procedures have undergone a sea change. There is a need to see how the deliveries can be sharpened, focused and how they are done in the days to come. Stricter regulatory norms have come into the picture. There are a lot of security concerns with the growing use of Information Technology and risk magnification needs to be handled by all bankers.

Future Focus Areas

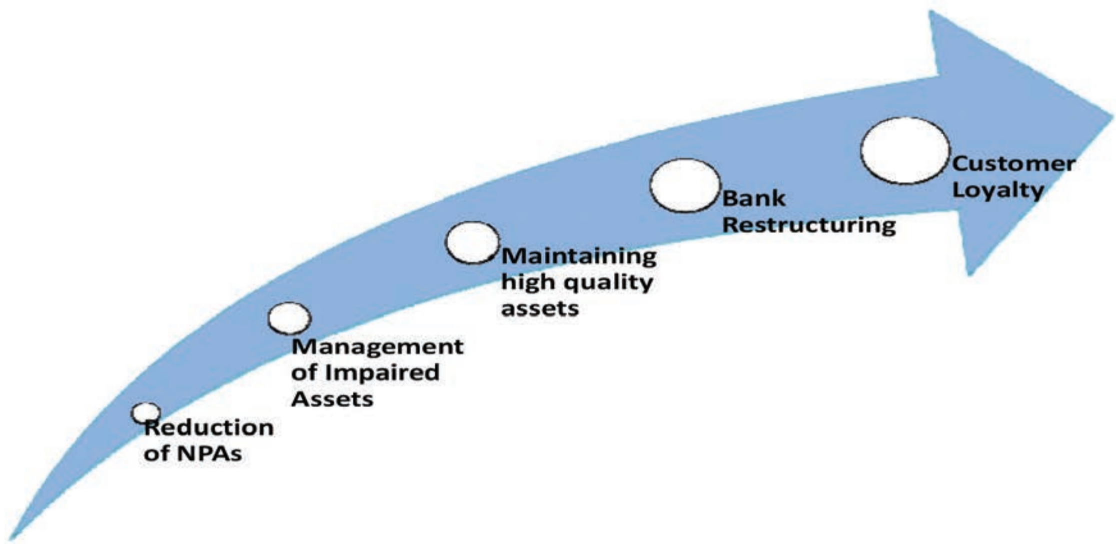
Compliance & Risk Management	• Building up a compliance and risk management culture at all levels of an organisation .
Growth	• Leveraging digital technologies, collaborations with other financial intermediaries
Payments Transformation	• Growth in contactless payments (cash—cards—digital payments) leverage customers' spending data
Data Management	• Big Data, Data Analytics, Chief Data Officer
Cyber Security	• Profile of CISO, clear and prompt communication with Board, timely detection and prevention of new threats,
Balance Sheet Efficiency	• Improvement in CASA, Reduce NPAs, Increase in NIMs, ALM
Consolidation	• Acquire synergy in operations, better bargaining power, better compliance with regulatory requirements.

Future focus areas include building up a complaint and risk management culture; leveraging digital technology, how banks will collaborate and role of financial intermediaries; the transformation taking place in the payments space; the large scale changes taking place in data management – big data, data analytics, etc., will become prominent and bankers will have to take full advantage of the tools available.

Some steps taken & suggestions

Product Innovation & Business Process Re-engineering has been introduced	Investment in online marketing & acquisition, Tie-ups with service providers	Mobile banking and Social media based transactions
Robust on-boarding program for new recruits, Performance linked Incentive Scheme.	Task Force to monitor Higher Value NPA accounts of the Bank	Recovery Champions identified in NPA concentrated branches
Data Analytics	Immediate online loan approval decisions	Increase efficiency and competitiveness

Challenges Ahead



Discussion Points

- Consolidation of banks
- Repositioning of banks with Entry of Small Banks/Payment Banks
- Delivery of services in branchless banking
- Capital requirement for complying with BASEL III
- Management of stressed assets
- Risk mitigation strategy to address technology obsolescence
- Prevention of cyber crimes and frauds
- Role of big data and analytics in changing banking environment
- Meeting customer preferences through technology and customer retention
- Implementation of online, mobile and social banking extensions to core offerings
- Cost effective e-Banking

Enumerating the challenges faced by the banking industry, Dr. Misra added, that any change is associated with challenges and it is up to us to face the challenges.

Dr. Misra said that the feedback received from banks on how they are positioning themselves and their thought process have been enumerated. Product innovation has assumed a lot of importance and business process reengineering has been introduced. Robust on-boarding programs for new recruits have assumed significant importance. Data analytics is also a focused area for many banks and they are taking advantage of this. Investment in online marketing and tie-ups with service providers has gained importance. An attempt has been made to include the suggestions of bankers as to how they propose to handle the new environment which they are facing.

Dr. Misra then drew attention to some discussion points which could be taken up from consideration by the eminent panel. He however said that the essence of the aspects would be left to the panel to discuss.

Mr. Arun Tiwari then set the panel discussion in motion.

Arun Tiwari: There has been talk of consolidation but of late there has been a spate of licences issued for payment banks and small banks. There is a banking paradox here - can payment banks substitute banks? Inspite of the accepted notion that banks may not subsist, banks will continue to play their role maybe in a different perspective?

Sourabh Tripathi

These are exciting times for the banking industry and India is the only country in the world where, in a span of three months, 20 new banks have been introduced in the market. Disruption is the only word to describe the situation.

By definition, payment banks are not allowed to substitute banks and guidelines state that payment banks have to lend in partnership with banks only and not in partnership with NBFCs, so the architectural set up ensures that payment banks work closely with banks to create a full product suite for the customer. The question is -will they really make a difference? Yes, through the very proactive regulatory intervention, RBI has managed to get certain types of unwilling players, the telecom companies, to participate in banking. The telecom companies, with massive presence and large customer base, have the ability to reach people and the ability to have relationship with people in large numbers.

This augurs well for the country. It will lead to new type of services, starting with technology driven and branch less banking. Also drawing in customers who are still outside the banking fold. This will also mean competition among them for the digitally savvy customers. The payment banks are also aware that to be financially sustainable, they have to reach out to the high-end customers who are digitally savvy. A recent survey conducted among 3500 customers showed that, only half of the digital banking customers in India were willing to try out the payment banks and only 35% of the customers who did not do digital banking, were willing to try out the new payment banks.

The existing digitally savvy customers will be the first to try the payment banks so there will be a heat and pressure on the new incumbents. The pressure is also on the existing banks to innovate and the next two three years will see a spate of innovative offerings. This will lead to a pressure on profitability and because there is pressure on profitability, there will be consolidation. These are two sides of the same coin:

- consolidate players who do not innovate fast enough and hence feel the pressure;
- introduce fresh blood into the industry to raise the quality.

Arun Tiwari: Any new venture would look at the commercial side also. With payment banks having to maintain 75% SLR and a cap of ₹ 100,000 deposit, will the new ventures find it profitable or would there be consolidation from the word go?

Sourabh Tripathi

Plain vanilla business is not very attractive for a payment bank. But there is an option value for the telecom companies. There is a huge benefit in the sense that a customer who has taken up the payment bank option will add or reduce their chunk of the business. If they fix a rate of return of 20%, probably 10% will come from the existing customer base and hence, they have to look to achieve a lower target.

With restrictions on partnerships, SLR constraints and only SB Accounts to start with – the new payment banks need to recognise the power of data - they will have the data on where the customer is transacting, payment information as to where the customers are banking, etc. Data is golden and in next 5 years, power of data will increase. It is essential for the service provider to get into a position which enables them to make offers beneficial to the customer and monetise the data.

It is likely that the customer may have term deposits with banks, but have SB Accounts with the payment bank and inspite of the limit of ₹ 100,000, move the transactions to payment banks. If transactions move away, the primary relations move away, the data about the customer moves away and the knowledge of the customer's behaviour moves away. That is the pot of gold, on which the payment banks will base their operations.

Arun Tiwari: Would you look at the licences as an opportunity for the traditional banks?

Rajnish Kumar:

Lot of small value transactions take place in branches, so cost of branch banking is very high. Ultimately, when payment banks come and they partner with banks, it will provide the last mile connectivity. Public Sector Banks have been responding well in introducing new channels and once the payment banks come in, particularly the telecom companies who have a wide reach; using them as Business Correspondents or Customer Service Points can give a lot of advantage. For instance, moving away low value transactions to payment banks or alternate channels. Going forward, the role of branches will undergo a change resulting in a productive gain for the banks by:

- giving value added services at high cost and thereby making it more profitable or,
- providing after sales service for the customer coming to the branch to ensure that they do not migrate to alternate channels.

Partnership and collaboration rather than competition is the way forward. However, payment banks cannot substitute the main bankers especially in the rural and semi urban space, where Public Sector Banks enjoy more trust. Serious money business will be driven by trust, built over a period of time.

The entry of the payment banks is a good development but questions remain over the revenue generation potential of payment banks. The revenue pool is not large and will come down further with competition. In developed countries too, where the banking space is occupied by 6-7 large banks, the new entrants have to make revenue by data mining or cross selling of other products.

Mr. Tyrone Chen then made a presentation on how talent management in banks are also undergoing a change due to the new paradigms. There has been a shift in demand for talents from traditional banking to digital banking. This change is evident even in the attire of the bankers and young bankers are ambitious for change.

Mr. Chen quoted from Brett King on building digital culture "Digital is not a department, channel or separate competency. It is simply the job of the bank and the CEO is the head of digital with a great team behind him that is fully committed. You can have some specialised competencies under this, but if you have a separate head of digital, you aren't a digital bank, you only have a digital competency within a traditional bank"

Mr. Chen added that in Taiwan, special emphasis has been given for the IT training of senior bankers to keep up with the changes. The top management is the guide/ explorer, the middle management developer and the solution providers for the senior executives. Also the branch managers are the professional advisors. The senior executives are the explorers for envisaging new opportunities; promoting changes and incentivising culture of innovation.

At the same time bank also has a functional team –

- being the innovator for designing client experiences creatively;
- leveraging the power of big data to unveil consumer behaviours from emotional, cultural and social aspects and,
- keeping a forward looking perspective on cyber risks and preparing for it.

  Regarding sales / service at the branch, Mr. Chen felt that the affluent need branches for increasing knowledge and hence, branches should upgrade and serve the people. Branches should become the advisor for:

- helping clients to get guidance toward adequate services,
- obtain integrated solutions specific to their needs
- take personalized financial advice.

  Since HR is at the core of transition it is necessary to allocate right people to the right positions and,

- define - professional competency at different functions.
- assess - potentials and gaps of knowledge and skills

- strategize - reallocate and put people in the right place; develop and train for growth; buy in and recruit talents from outside of banking.

  Mr. Chen explained how Taiwan Academy of Banking Finance has incorporated Bank 3.0 by:

- blending training with certification to develop and identify high potentials.
- evaluating the adequacy of talent resources at key positions through professional competency assessment.
- partnering with universities to explore and furnish e-banking talents at early stage.

Arun Tiwari: The presentation was lucid explaining the architecture and role of TABF in banking in Taiwan.

The power of data. Historically, banking space has been occupied by Public Sector Banks. But, are they capturing the data the way it should be and if they are, are they harnessing the data in the right manner? Looking forward, what is the role of data analytics in the future?

Sourabh Tripathi:

The leading banks in the world are also struggling for cutting edge with data, because technology is moving fast. Banks have made tremendous strides in the last few years, yet the institutions find that they are not able to get all the data that they want, capture all the right information that they want. Problems are the same the world over and not restricted to Public Sector Banks. As regards use of data, we are sitting on the most underutilised data – basically, the banking behaviour of the customer known only to the banks. Going forward, through mobile banking, the bank can even know where the customer is at a particular point of time. The possibilities are limitless. Plain vanilla banking is going to become commoditised.

But at the same time, banks will have pressure to maintain profitability; create value added offerings, in the form of advice to the customer; use data to compare the customer to others like him/her, etc. One side of the coin is that banks are trusted and have the data, so they should use it to further their business and on the other side, with the data available, it is necessary to engage customers and become real partners to the customers in terms of their financial well-being.

In this context, he shared the example of Brett King, the author of 'Bank 3.0' and the co-founder and CEO of Moven, a New York-based mobile banking startup. The app provides real-time updates for debit card purchases and warns the customer when they have reached their upper limits.

Data analytics provides huge potential for credit. Banks can use the data to give credit. Alibaba is an example of an entity which lends to people totally unrelated to their business but their NPA levels are 1/10th of the banks, thanks to the power of data. Basically, technology is there just to support the usage of data. Therefore, the moot question is not "are we capturing all the data, but are we utilising the data captured?" The answer is an emphatic no. There will be more avenues to come in the future and the banking sector should be prepared for it.

Arun Tiwari: SBI's Intouch, how has been the experience and going forward, what is the role of social media in the banking space?

Rajnish Kumar:

Intouch has been a very good experience for our customers and it is a novelty. Soon, majority of the branches in urban areas will be in the Intouch format. In future, branches have to be designed keeping in mind what type of customers are coming in and Intouch will be popular with the younger generation. In social media banking, there are lot of behaviour patterns which can be captured and which can play a critical role in assessing the needs of the customer - real time, based on their behaviour. Also critical inputs regarding the credit and financial decisions, can come through social media.

Arun Tiwari: Ultimately, when we talk of technology in a service industry like banking, we talk of cost effectiveness and the ease of doing transaction from the customer's point of view. When we talk of consolidation of banks, in respect of banks working on the same platforms in terms of technology, why these facilities should not be consolidated?

Rajnish Kumar:

There are models, like mortgages, where companies provide shared services. Abroad, banks outsource their mortgages. But there are regulations and stringent secrecy laws to be complied with. The customer's sensitive information has to be protected at the bank and, hence, it is very difficult to outsource the core services. But in case of supplementary services like Internet banking applications, mortgage applications, loan servicing/collection, if the systems of the service provider are very strong it can be a very effective model.

Some applications have ready platforms like customer service management.

The debate rages on within banks how much to keep within and how much to outsource. Security considerations and confidentiality of data make it necessary for banks to be very careful of the entire system and ensure that there is no data leakage or compromise on the security aspect.

It is a feasible model. But in India, the service provider may be the same for several banks, but the products are customised and it is not possible to create clones. When it comes to consolidation/merger, commonality of key platforms would be a key consideration but will not be a deal breaker.

Sourabh Tripathi:

The consolidation of banks in India has been much talked about but has not really happened. This is because the underlying logic is not clear. The consolidation talks are driven by HR/talent and not by the fundamental issues of banking. Across the world, banks continue to merge and they have different technology platforms, so that is not an issue. In India, the cost of technology is 1/5 to 1/10 of the cost of technology for the banks in the world. So banks in India spend 2-4 % of their revenues in technology whereas the banks in the west spend 15%. Also, the most technologically advanced banks in India have only 1/4 of the number of people that the comparative banks in the world have. It is true that there could be a lot of benefit by sharing technology and cloud based software will be used for many applications in banks in the future and will reduce the cost dramatically.

Another interesting trend noticed in the west is that the banks are increasingly insourcing technology, since technology is the unique competitive advantage. If a bank buys a mobile application from a vendor and other banks also buy the same, the applications will look similar and hence, the new trend is that the lower standardised platforms (core banking solutions) are outsourced but, the applications which are customer facing and applications which are employee facing are kept in-house because that is the source of competition, and it would be advantageous if the bank can change it as and when required and not wait for the vendor to change it.

Banks are, therefore, creating innovation centres where they create an environment where best technology would come. ING Bank Netherlands has recognised that to attract the best talent and give them the best, which the software industry offers, a new environment/ unit would have to be created outside the bank with different HR policies, so that the new talent works in a different and less hierarchical organisation. Banks therefore are progressing towards creating a core team of technologists, who can be the source of differentiation.

Arun Tiwari: Banks in Taiwan - to what extent technology is playing a role in delivering banking services especially in the smaller towns?

Tyrone Chen:

There are 30 banks in Taiwan, which implies ‘over banking’. Consolidation exercises have also not worked with banks unwilling to merge. Therefore, the Govt. made a solution – they created a Credit Information Centre, 40 years ago. Here, the information about the credit availed by the customer is maintained to enable banks to avoid frauds or multiple credit to fraudsters.

Digital banking in Taiwan also faced the same issues as the world over. Small banks did not have the funds to embrace technology in a big way. Government therefore established the solutions separately, for instance the ATM Solution Centre, a platform which could be used by small banks and those concentrated in the rural areas. They also established Centralised Information Centre to provide IT solutions to small banks.

Arun Tiwari: Gyan Sangam to Indradhanush – Govt. is talking of consolidation for last 10-15 years. A few mergers have taken place in the past in Public Sector Banks but the Govt. feels that the consolidation should come from the banks and should not be imposed. Consolidation should be based on size or efficiency? Going forward, would there be consolidations or new banks?

Rajnish Kumar:

In Public Sector Banks, all consolidations/mergers in the past have taken place because of the likely failure of the merged bank and have been mooted by RBI. Why should banks merge? Unless that is clear, mergers cannot take place. We need strong banks to cater to the growing needs of the corporates. But the capability of the existing banks to meet their requirements is limited. At the same time, merging a weak bank with a strong bank is not the answer. Again, if ESOP comes, then new questions will emerge - the economic consideration of the merger, whether the value of the shares of the combined entity is going to go up and if it would be in the interest and benefit of both the entities. In India, unless there is a nudge from the Govt., consolidations are not likely to happen voluntarily.

Arun Tiwari: Capital requirements under Basel III was triggered by crisis in US. When the prescription is in place why do we have stringent laws? Capital is needed, but capital to what extent and capital at what cost?

Sourabh Tripathi:

RBI always adds a layer in addition to the international prescriptions. This is because the conservative stance helped India in the recent global crisis. Developing economies like India are riskier, and hence, higher levels are required. In a rapidly growing political environment with multiple pushes and pulls, it is an inherently volatile situation and hence the risks will obviously be high. The higher cushions are likely to hurt the banks but are necessary in view of the higher risks.

Rajnish Kumar:

If we analyse, till 1992, the banking sector was highly regulated, be it credit or interest. Hence, there were no innovations and consequently no credit risk. Inherently, the Indian psyche is to plan for risk. On the negative side, it does not allow innovation. On the other side, innovation in the western world is far ahead. The positive tendency enables us to withstand shocks and the negative stifles innovation.

From looking upto RBI at every stage, banks are now slowly moving towards a phase, where they are developing their own risk framework and working according to a plan. It is true the incomes are under pressure and for banks to provide for loans, they need to look at external factors also, especially macro-economic factors which affect bank credit. There are certain inherent weaknesses in the risk management practices of banks and the management of loan assets weighs in the minds of the regulator when it prescribes higher levels of capital.

Arun Tiwari: There is a contradiction in the prescription of the regulator - SLR is 21.5% and still there is talk about Liquidity Coverage Ratio. Secondly, as per the Basel III requirement, the enhancement in capital requirement needed may be partly funded by Govt. (₹ 25000 cr.), which may not be sufficient going forward in the next three years. Also, in next five years, Govt. feels that the funds can be raised from the market. Do you feel, once the economy picks up and keeping in mind the kind of money which would be needed for our capital, would the banks be able to generate that?

Rajnish Kumar:

This appears difficult. The banking sector makes money by taking risk and leveraging was one of them. As the Balance Sheet is leveraged and more stringent requirements under capital adequacy frameworks come, the Return on Capital will not be as it was earlier. Internationally, the Return on Capital for banks is between 6-8 % and hence, it is not profitable for banks to approach the markets for capital with such low returns. It is a Catch-22 situation.

For banks in India, raising funds from the market is going to be difficult. This year because of the falling commodity prices, particularly oil and energy, there was headroom available and Govt. could provide for capital but going forward, it is difficult to say if that will always be the case.

Raising capital from the market is going to be difficult unless the profitability increases and profitability cannot improve unless the asset quality improves and the provisioning costs come down. At present, the Return on Assets is around 50 basis points for most Public Sector Banks and Return on Equity not more than 9-10%. In such a situation, going to the market and asking for investments will prove futile, because, who is going to invest at such low rates of return? It means that the task for all the bankers is vast- they need to look at each and every activity from the perspective of Risk Adjusted Return. Banks cannot afford to blindly follow each other and only focus on growing the Balance Sheet. Each and every account should be mapped and should meet atleast the average cost of capital. So, risk adjusted capital has to be equal or more than as of now. But in reality, that is not the situation. This is a concept which is in a developing stage and will need fine tuning. One of the factors has to be adjusted - find the capital for growth or give leverage and have the Balance Sheet size for weighted average of capital assets.

As regards LCR, SLR is very high in India and amongst the highest in the world. With regulatory controls and interest controls on advances, banks have tight liquidity to move around.

Sourabh Tripathi:

Market capitalisation will improve if the market believes. But the market does not believe that the Government will really give autonomy - to talent management and to let the Public Sector Banks be run professionally. If this happens, that is when we will stop worrying about capital and till the Government is not ready to bite the bullet, we will continue to have this perennial worry.

Arun Tiwari: How well capitalised are Taiwanese banks? Are they adequately capitalised or is there a problem of capital adequacy in most of the banks?

Tyrone Chen:

Banks in Taiwan face a severe competition. The spread is very low and hence the banks have to struggle to raise funds from the capital market. Government of Taiwan and the banks are looking at other possibilities and many banks have taken the route of mergers. But there is still a long way to go.

Arun Tiwari: Stress portfolio of assets- in China they pooled all the assets which was capitalised by the Govt. Immediately thereafter, the top four banks entered the market and whatever premium they got from the issue was returned to the Govt. So it was remunerative to the Govt. Can we think of something on similar lines in India?

Sourabh Tripathi:

There is one line of thinking which is against this idea, that there is a moral hazard (the orthodox thinking). They feel unless there is a crisis, this should not be resorted to and should be sorted out by the institution themselves. There is some pressure to see where there is room for improvement, but the orthodox thinking will prevent this idea as being the only idea to solve all the issues.

I feel that we will do it. We will create such a bank, but only part of the assets will move there and not a large amount, which will create a relief. Some of the things will stay in the bank books and banks will have to take care of that. The idea will take time to come to fruition in India and hopefully by the time the idea takes shape, the need for it will be less.

Arun Tiwari: 55-60% of the stressed assets are in stalled projects- roads, ports, steel plants, power plants. Gas was promised - not given, right of way- not given. Even in projects where 80% of the work is completed, there are several issues which crop up. Who is to be blamed in such situations? The pain is more for Public Sector Banks who have to follow the process which will take its own time. ARCs take their time. They have given 15% but, we are yet to see any resolution in last two years. 1.5% management fee is paid every year and at the end of 5 years, the banks will pay out whatever they have given and then the banks are back to square one. Do you feel going forward in a year or two there could be a brighter side for the resolution?

Rajnish Kumar:

I hope so. Much of the hopes of the banking industry is being pinned on the new bankruptcy laws which is being talked about and which is likely to be tabled in the Parliament in the coming Session. Creating a bank for recovery will not work unless you have a proper recovery and resolution mechanism. There are reservations about its practicality. When the sectors were opened up in infrastructure particularly power and roads, there were no options but Public Sector Banks had to support. All the DFIs disappeared from the scene. It was also seen as an opportunity for banks and even looking at pricing and interest rate, there were better margins, better upfront fee. When all these loans were given, it was with the expectation of better returns but, many projects ran into difficulty because of environmental issues, encroachments, etc.

But the biggest problem came in the power sector. Core industries like steel have also been financed by banks and they have been a cyclical industry. Unfortunately, they now have a bad cycle which has been much more prolonged. In the power sector, the problems are mostly around the reforms of the Discom. Fuel availability has improved and cost of gas has also come down and Government has given support and has tried to ensure that the tariffs of the gas based plants are almost at par or at the most 20-30% higher than the traditional thermal power sector. If the power sector reforms are to happen and if the Governments (Central and State) are able to tackle the Discoms, that will be a big positive for the power sector.

The projects are all good projects and many started in 2010-11 have been commissioned and they will start supplying power soon. PPA is a problem because Discoms don’t have the money, they don’t have money because the transmission and distribution losses are very high. For the power sector, the solution lies in the Discom reform and to add to it in the last three years, no new projects were announced in the thermal sector. So in 2-3 years’ time, the power prices are likely to go up. A project conceived today cannot be commissioned before 2022-23. All these projects which are in the private sector were conceived in 2008-09. Projects got off the ground in 2011 and now in 4-5 years they are ready to be commissioned. There has been some action in renewable energy, but as a percentage of the overall power requirement, their contribution is limited. So that is not going to make a big dent. Ultimately, I am positive for the power sector but we have to wait for one or two years.

So the key lies in power sector reforms, faster recovery and resolution where there are effective bankruptcy laws and the working of the Debt Recovery Tribunals. Courts also need to intervene less in these matters. In UK, mortgages are enforced in 15 minutes and decision making is fast. In India, the enforcement of mortgages under SARFEASI takes forever. The bankruptcy law and the functioning of DRT is very crucial. This coupled with the fact that banks need to improve the due diligence process. Lot of improvements in pre-sanction and post sanction monitoring is also required.

The forum was then thrown open to the audience for a Question & Answer session.

Question: Efficiency of the banking system- In India the spread is around 3 %, in Taiwan the spread is around 1.5% and globally, it is around 1%. With ₹ 25,000 crore needed to meet Basel III, how will the whole yield process look like in the next decade? In the next decade or two, what will be the fate of the large Public Sector Banks with the new technology coming?

Sourabh Tripathi:

To answer the 2nd question first. What will happen to Public Sector Banks once digital banking comes? The latest research shows that only 13% of the people in India use any form of digital banking today. The rate of adoption of digital banking is 2-3 years behind the rate of adoption of online shopping, etc. People don't adopt digital banking so quickly and so in the next 5-10 years, bank branches are not going to go away. 90% of the people are out of the fold of digital banking and it will be a long journey to bring even 50% of the population under digital banking. Getting rid of branches is therefore not easy.

Even internationally, the branches will remain. May be in different forms. In the banking industry, there is need for human interaction, and therefore need for branches. There are very few markets that are digitised and where everybody feels comfortable to do digital banking. In India, banks like SBI are trying to do many new things on technology, digital banking, etc. The relevance of branches will therefore remain.

To answer the first question - in emerging markets, banks have high NIM. Some of the researchers believe that is how it should be. In an emerging market, if the NIM is low, it is an injustice to the banking industry. The risks are higher, the inflation is high, and the interest rates are higher. The high rates of SLR and other requirements force the Indian Banks to operate at higher NIM. We are however nowhere close to where Indonesia is. Indian Banks have a moderate NIM. It should stay that way also because if the NIM is disturbed, the banking industry's ability to innovate and progress will be hampered.

Rajnish Kumar:

As far as distribution network is concerned, establishing a distribution network like SBI has today, is an envy for other players. It is not easy and the role of the branch is definitely going to undergo a change as more and more low value transactions move out of the branch. Although we have a BC model, we will still need a branch where many of the customer service points run by the BCs will be managed. Apart from that, the branch not only does banking but also selling of insurance products, mutual funds, etc. After 5-6 years, perhaps the branches will become the point of cross selling of products. Branches may also become delivery points for the e-commerce sites.

Branch banking has the highest cost per transaction, so the branch has to look at value added services/ advisory services, where they can reduce cost of branch banking. All the channels are likely to co-exist and any new strategy will probably look at an integrated channel: how many brick and mortar branches, ATMs, Internet and Mobile Banking. Earlier it was handled separately, in different silos- branch banking was done by a different department, digital banking by a different department, etc. Now it has to be an integrated approach and for five years atleast, the brick and mortar will continue. The question will be how many brick and mortar branches, what type of business is to be done at these branches and what type of business is to be migrated.

Ultimately, the customer is the king and it is their choice what channel they want to use. Beyond a point, we cannot push the customer to any particular channel. Even today, many customers still prefer branch banking and Public Sector Banks still welcome them and give them service, even if it is high in terms of costs. In several developed economies, the customer has to pay for visiting branches. But we are far away from reaching that stage.

Question: Rigid NPA norms are being followed now. Should we not have region wise NPA norms

monitored by RBI instead of having one impractical norm for the entire banking industry, which is affecting not only the bankers but also the entrepreneurs?

Rajnish Kumar:

The 90 days' norms have been internationally accepted. When an 'out of order' account or 'overdue' account is identified, internationally it is accepted that it is an NPA account and deviating from that criteria is probably not going to be acceptable and will put a lot of doubt on the credibility of the Indian Banking System and so we have to live with that norm. What is happening in India is that, it is the only norm which we are following for declaring an account as NPA whereas, in any other jurisdiction like, Singapore or USA, the asset classification can be treated as an NPA even if there is servicing of interest and repayment of principal is not in arrears. They look at the fundamental weakness in the account and not only to the account being overdue.

Question: We are talking of the transformation of the brick and mortar branch into the digital branch but who will be the driver for such projects? Where will the talent for operating the new strategies come from? Given that other sectors are better paying.

Do you think the stringent regulations laid down by RBI (inspite of the fact that the Indian Banking Industry was not affected by the bubble burst) are because they are unable to control the Banking industry effectively, mainly the people who run away with bank's money?

Arun Tiwari:

Beyond a point it is not the perks, whatever you get as a professional, you earn and slog and what you get, that defines the job a person does. Talking about the talent, IIMs and IITs, although they do not have world class facilities, do give some of the best to the industry as is evident from the fact that many corporations globally are headed by Indians. At the lower level when we talk of the talent in the banking sector - people are ready to come to Public Sector Banks because of the 360 degree exposure that they get in Public Sector Banks. Permanency of jobs is another reason why they prefer to come to Public Sector Banks.

Sourabh Tripathi:

There is a very large workforce in Public Sector Banks who are very dedicated and give their all to their institutions. However, this is not sustainable. When the young generation joins Public Sector Banks, they will not stick around, particularly when twenty new banks are around. The young generation will gain all the experience and go. There is no other way but to open up the HR policy of the Public Sector Banks. In contrast, the Public Sector Banks in many other emerging markets are powerful and also doing very well. The top ranks are appointed by the Government but their salary is not linked to the bureaucrats' salary.

Rajnish Kumar:

The industry level bank settlements should be done away with. Each bank should have a separate pay structure depending on their own capabilities. Flexibility should be allowed but is possibly not wanted by the Bank Management. Studies show that Public Sector Banks pay better than Private Sector Banks upto scale IV and it is only when one moves up the chain that the remuneration go down. The ratio between the entry level salaries and the salaries of the top management is skewed. At the same time, in developed economies, the difference is extremely skewed. Therefore, the need of the hour is for performance linked incentive.

Question: Banking research is a well-recognised and developed profession in advanced economies. In India, research in banks means economic research. How much banking research are we doing in banks – regarding private/public; foreign exchange/investment banking; behaviour analysis of customer for digital banking, etc. Because technology is moving very fast, unless the financial literacy is improved, there will be human and technological frauds. In advanced economies, they are investing a lot on cyber security. How many banking research institutes do we have in our country? This job should be taken up by IIBF. Atleast the study of the people taking the exams can change the examinations system.

Dr. J N Misra:

IIBF is mainly in the certification area. We do sponsor research but do not have a separate research wing. Going forward, we may have a wing separately. The large banks should ideally be having this Department as part of the innovation centre set-up. This is how it will translate to banking business.

Rajnish Kumar:

To split the question- when we talk of the role of credit in taking credit decisions - for corporate banking, macro-economic research, the research on the specific industry and the client all together become relevant.

Where retail banking is concerned, behaviour pattern and analysis of data becomes important and that capability has already been created. Wherever there is mass banking, the role of data is very important, which will speed up the decision making process and that will give confidence to the people taking credit decision or approve using data analytics. This is being introduced in banks and there is a good progress in this direction in many banks.

When we come to development of applications which are customer friendly - there are lot of innovations which can happen from the inside. IT architecture should be such that it provides the necessary flexibility to use the talent pool available in-house.

Mr. Arun Tiwari thanked the Panellists and the audience for an interesting and stimulating session.

Payment Banks and Small Finance Banks

Payment banks have the primary objective of financial inclusion through providing small savings accounts and payment/remittance services to the migrant labour workforce, low income households, small businesses, other unorganised sector entities and other users, by enabling high volume-low value transactions in deposits and payment / remittance services in a secured technology-driven environment. Payment banks are not allowed to undertake lending activities and will be restricted to holding a maximum balance of ₹100,000 per individual customer initially. Apart from amounts maintained as CRR with the Reserve Bank on outside demand and time liabilities, these banks will be required to invest minimum 75 per cent of their ‘demand deposit balances’ in government securities/treasury bills and in other securities with maturity up to one year that are recognised by the Reserve Bank as eligible securities for maintaining SLR and hold maximum 25 per cent in current and time/ fixed deposits with other SCBs for operational purposes and liquidity management. The 11 applicants who have received in-principle approval for setting up payment banks propose to bring fresh capital of ₹ 16.22 billion to the banking system and an addition of 1,140 bank branches in their first year of operation.

The objective of setting up of small finance banks (SFBs) is furthering financial inclusion by (i) providing savings vehicles primarily to unserved and underserved sections of the population, and (ii) supplying credit to small business units, small and marginal farmers, micro and small industries, and other unorganised sector entities, through high technology-low cost operations. SFBs have a priority sector lending target of 75 per cent of adjusted net bank credit (ANBC) and at least 50 per cent of the loan portfolio should comprise of loans and advances of up to ₹2.5 million. The 10 applicants who have received in-principle approval for setting up SFBs propose to bring fresh capital of ₹57.34 billion to the banking system and an addition of 2,444 bank branches in the first year of operation.

A working group has been formed to examine and finalise the regulatory and supervisory framework for payment banks and small finance banks. The group is currently examining the various issues that need to be addressed considering the size and scope of these banks.

Source : Financial Stability Report, Issue No. 12, Reserve Bank India, December 2015

2nd Session: Inclusive Banking Experiences

Theme presentation: Mr S. Muralidaran, Director (Academic Affairs), IIBF

Panel: Chair: Mr. M V Tanksale, Chief Executive of Indian Banks' Association (IBA).

Mr. H R Dave, Deputy Managing Director, NABARD

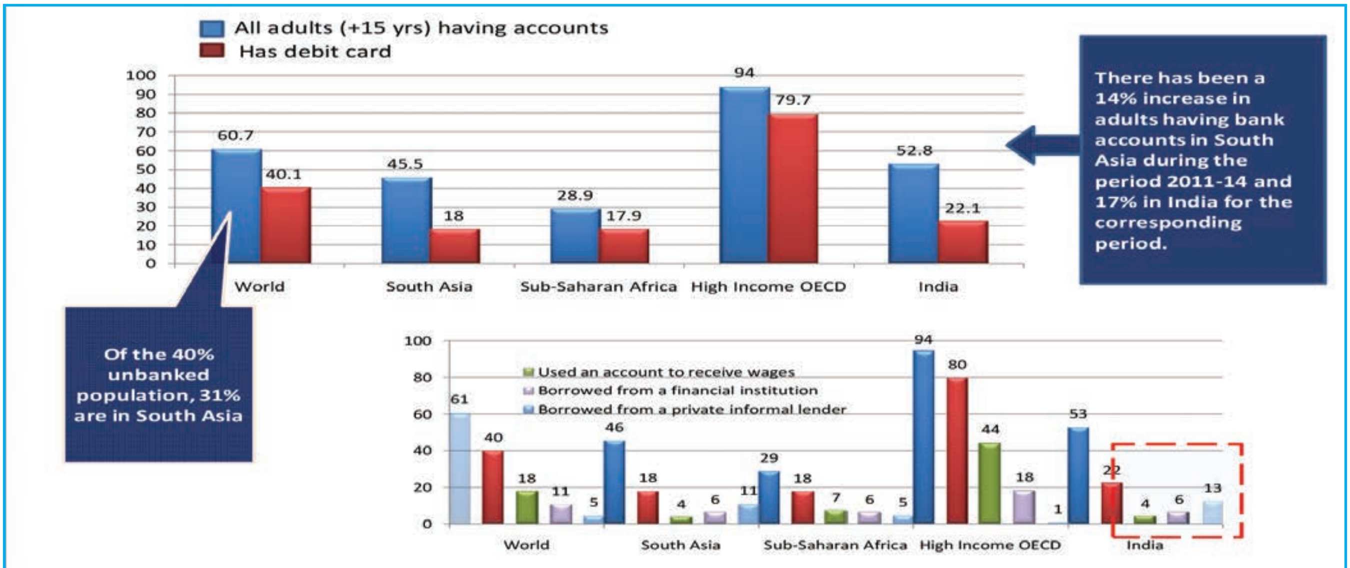
Mr. Pramod Kumar Panda, CGM, RBI and Principal of College of Agricultural Banking, Pune.

Dr. Shah Md. Ahsan Habib, Professor and Director, Training, Bangladesh Institute of Bank Management.

Present Outreach

No. of Bank Branches (31.12.2014) Rural 47278 Semi urban & Urban 55129 Metro 19887	122294
No. of account opened under PMJDY (09.09.2015)	182 million
Balance in PMJDY accounts	Rs. 237 billion
% of zero balance accounts	43.12%
No. of ATMs (31.12.2014)	176,409
No. of Post Offices (31.03.2014)	154,882
No. of Fair price shops (apprx.)	500,000
New Payment Banks	11

Source:
http://financialservices.gov.in/banking/FinancialInclusionIndicators.pdf
http://www.pmjdy.gov.in/account-statistics-country.aspx
http://www.indiapost.gov.in/our_network.aspx
https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=34754



Source: https://openknowledge.worldbank.org/bitstream/handle/10986/21636/9781464805523.pdf?sequence=3

Mr. Muralidaran introduced the panel members and presented the background for the panel discussion and set out the important milestones of the past.

Initiatives like nationalization of banks, Lead Bank Scheme, Establishment of Regional Rural Banks, formation of Self-Help Groups, PMJDY were all aimed at deepening financial inclusion efforts.

Attention was drawn, to the achievements under the various initiatives of the Govt. and the regulator. The outreach of banks, institutions and other agencies is quite impressive; but financial exclusion still exists. The initiative taken by Government of India under PMJDY has provided additional impetus for achieving financial inclusion. 182 million accounts have been opened

Barriers to Financial Inclusion

DEMAND SIDE	SUPPLY SIDE
Low literacy levels	High fixed costs/bank charges
Irregular income leading to frequent micro transactions	Low income population not attractive
Lack of trust	Concentration on economically active population – middle of the pyramid
	Dormancy of accounts
	IT Security
	Lack of awareness among the villagers on the Government benefit schemes

Financial Literacy Centres and Consumer Protection

Operational FLCs (31.03.2015)*	1181
No. of activities conducted (during 2014-15)*	84,089
Total no. of participants*	52,38,358

- Financial literacy, through :
  - ✓ courses in schools,
  - ✓ literacy camps organised by banks and RBI, or
  - ✓ newspaper or social media campaigns,
- Raising the level of acceptance of technology by customers
- Consumer Protection/Customer Service:
  - ✓ Covering newly included and typically unsophisticated customers
  - ✓ be easily accessed and have speedy grievance redressal process
  - ✓ Should raise customers' awareness about their rights and duties

*https://rbidocs.rbi.org.in/rdocs/AnnualReport/PDFs/00A157C1B5ECBE6984F6EA8137C57AAEF493C.PDF

Role of Technology in Inclusive Banking & Future Road Map

➢ Packaging of PMJDY - Debit card with default accident cover and life insurance provisions and possibility of an overdraft.

➢ Enrolment of UID and eKYC enabled bank account; technologies with multi-faceted options for instant account opening through eKYC,

➢ Platforms which have the ability to support eKYC, Aadhaar based transactions, and Rupay Debit cards with Pin and Biometric based authentication

➢ Diverse delivery channels such as Smart Cards, biometric ATMs, Point of Service (PoS) devices, tablets and mobiles.

➢ Raising the level of acceptance of technology by customers

➢ Direct Benefit Transfer has provided a big fillip to Financial Inclusion

Prime Minister's Twenty year vision:

Reserve Bank of India to draw up a 20-year roadmap aiming for full financial inclusion by 2035. Prime Minister has asked the Central Bank to identify milestone years for achieving the financial inclusion targets.

Views of Banks

- A dedicated toll free help line number in SLBCs for redressal of grievances (PMJDY).
- Survey of all households in allotted villages to ascertain households who don't have bank account.
- Penetration of FLCs from District level to Block level to reach rural population.
- In house training of all staff on Financial inclusion
- Honouring best performing bank mitras every year

Concerns & Suggestions:

- Increasing NPAs in banks not allowing banks to transmit policy changes by regulator to customers totally.
- Interest rates on other savings schemes should be taken into consideration before lowering ROI on deposits.
- Banks should adopt technology-based solutions for managing risks such as Reputational, Operational and Financial Risks under BC model.
- Financial Literacy to involve players like insurance companies, PFRDA to create awareness among people about importance of need for social security net in the form of micro insurance and pension after superannuation.

under PMJDY; the balance in these accounts being ₹ 237 billion. RBI has also given an in-principle approval for 10 small finance banks. These are also expected to strengthen the financial inclusion efforts.

Seen from a global persective, large differences exists in regard to having accounts, debit cards etc. between High Income OECD and other countries. There is a need to bridge this as early as possible.

Mr. Muralidaran added that there are barriers to financial inclusion both from the demand and supply sides. Both

Discussion points

- Why 100% Financial Inclusion has not been achieved so far?
- Focus of Financial Inclusion has perhaps been from supply side and not demand side
  - Are Financial literacy programmes for deepening financial inclusion an answer to demand side push?
- How to deepen Financial Inclusion?
- Viability of the BC/BF model. What are the risks involved in this model?
- Is the BC model the most appropriate for financial inclusion? Are there better models?
- New bank licenses; payment banks/MUDRA Ltd., and its impact on Financial Inclusion
- Role of technology in Financial Inclusion– including security issues, connectivity, communication etc.

need to be addressed. From the demand side, financial literacy will play a crucial role and from the supply side, technology will play an important role in deepening financial inclusion and will play a crucial enabler to reaching the unbanked in a most cost effective, scalable manner.

There are 1181 FLCs as on 31.3.2015. FLCs will play a crucial role in-so-far as financial inclusion from the demand side is concerned. Raising the level of acceptance of technology by customers will require sustained financial literacy initiatives on the part of bankers. Involving other players like Insurance Companies, PFRDA etc., will provide an added fillip to financial literacy efforts. Customers' awareness about their rights and duties is integral to developing a conducive consumer protection environment. This will also necessitate banks to develop strong internal grievance redressal mechanisms.

Technology is expected to be the agent which will give the thrust to the Financial Inclusion Initiatives.

The above are some of the steps taken by different banks. Very good steps have been taken. There are concerns as well in the form of increasing NPAs, difficulty in lowering rates of interest on deposits, risks in BC model etc.

Mr. Muralidaran then flagged off some of the discussion points mentioned above for the panel to deliberate.

Mr. M V Tanksale then set the panel discussion in motion, by drawing attention to the long relationship between the IIBF and IBA.

M V Tanksale: I have seen the evolution of the banking sector in the last four decades, having been closely associated with it, beginning with the nationalisation of banks, the thrust on rural banking, opening up of the branches in the rural areas, a couple of milestones, like creation of NABARD, and the policies on the Business Correspondents and Business Facilitators, etc. The banking industry today in India is an industry with 120,000 branches operating in the country. The regulator has also recently given licences for 11 payment banks and 10 small banks, but the challenges of the country are different. India is a nation with 660,000 villages wherein, the population of many villages is below 2000. Therefore, there is definitely a challenge of access, challenge of delivery and communication. RBI has embarked in a structured way from 2006 onwards and the Financial Inclusion plan I and plan II followed. Today, through the PMJDY which is driven by the Government of India, through the banking industry, banking is claimed to have reached each and every household in the country. 182 million accounts have been opened under PMJDY and if the financial inclusion figures were seen from 2006 onwards, they would be in the range of 400-500 million accounts. But inspite of the number of accounts opened by the banking industry, is the financial inclusion merely an illusion of the banking industry or much beyond that?

I will now draw attention to the first question - Why 100% Financial Inclusion has not been achieved so far? Although the financial exclusion in developing countries is far more than the developed countries, where the financial exclusion maybe below 10%, the focus on Financial Inclusion in all the nations is the same. At the same time, on the financial literacy front, there is great thrust, and especially Asia Pacific countries will have to address these issues slightly differently given the challenges of volume, geography, etc.

NABARD is a revolutionising institution for the co-op sector and the Regional Rural Banks and really close to the grass roots. We have not really achieved 100% Financial Inclusion. How and when do you think we will be able to claim that we have reached 100% Financial Inclusion? And what exactly do you define as 100% financial inclusion?

H R Dave:

From NABARD side - the Financial Inclusion perspective runs into three parts:

1. NABARD needs to be a facilitator of the entire nation but how will the facilitation take place?

2. How do you see the integration of the large microfinance movement in which the country has invested substantially - financial and human resources, putting together almost 77.7 million SHGs. Is there a possibility of converging the FI efforts on the microfinance sector?

3. Gamut of Financial literacy - on the demand side, financial literacy plays a major role and we need to see how the issue is to be addressed.

The three broad spectrum approach:

1. The facilitation part- the way the financial inclusion landscape has evolved in India especially after 2014. Since the new Govt. has taken over, the focus on the demand and supply side has been equalised.

Initially we thought that we were primarily focusing on the supply side of it - enabling banks, directing banks, supporting banks to reach out to the people who have not been reached out. But the Govt. made the people look at what is being offered by the banks more seriously by taking the no frill account and bundling it with certain other incentives. Where earlier, the branches were going to the villages, the crowds have now come to the branches. There is a subtle shift but a major strategic shift in terms of how we reach out to the people.

The supply side part, the 350 odd rural co-operative banks and 100 + PACs, unless these institutions are brought into financial inclusion landscape, efforts of the entire industry will be incomplete. So NABARD put all these banks on the CBS platform and now these banks are moving towards providing Rupay cards, RTGS, mobile banking, internet banking etc., and we believe that in another 2 years' time most of the co-op banks, which are strong enough to get approvals from RBI, will be in a position to offer the add on services.

2. We have also enabled the RRBs, in putting the systems in place and assisted the RRBs, especially the weak RRBs, to take care of the CBS expenses.

3. We have now launched a massive exercise of digitising the SHG movement.

Half of India's population is linked to the banking sector through the SHGs. The Bank Linkage – SHG programme, is by far the largest microfinance project in the world. The issues in the Bank Linkage – SHG programme today are known to all. Unless they are Aadhar enabled, unless they are put on the digital platform and unless they are linked to the credit bureaus, the issue of repayments, poor quality of maintenance of accounts, multiple finance will continue to be reasons for the growing NPAs. The NPAs in the SHG – bank linkage programme is somewhere between 7.5 and 8% which is leading to real issues, and rethinking on the part of the banks.

Efforts were being made to bring the SHGs into the fold by self-managed, doorstep financial inclusion system. But the difference was that there was no technology. SHG- bank linkage programme and technology remained apart. Efforts are now being made to place them on the technological platform. Every member of the SHG will be Aadhar enabled, they will have a savings account, the DBT mechanism for women oriented transfer benefits will be routed through this account, the SHGs books of accounts will be maintained through the digital platform and they will also get returns. Importantly, at the rural branch, the branch manager who handles 100-500 SHGs and who does not have the time to monitor the SHGs individually, will now get a MIS report on the SHGs, which tells him what is happening at the SHG level.

M V Tanksale: We will now take the technology part forward. While NSCI gives a perspective of the capacity building requirement, and what is it that is driving it? The biggest challenge is how do we get capacity building for the BC agents and the BFs who are actually an extended arm of the banking industry? To make the whole programme viable, they will probably have to put on some kind of measuring scale on the efficiency, productivity, etc. What is the perspective on the gap and the capacity building?

Pramod Kumar Panda:

RBI is probably one of the few central banks in the world over which has been talking about, thinking about and acting on financial inclusion much before the whole world started talking about it in an active way. The initiatives undertaken by RBI includes the setting up of CAB, in 1969, as a college for Co-op banking, that was later on converted into CAB where bankers were trained and skills were deployed in agri related areas. The regulatory initiatives were both in the nature of broadening the banks and giving them some kind of direction. The priority sector lending guidelines of RBI were fundamentally in the nature of financial inclusion drive, which at that point of time was not articulated in that language. People started talking about financial inclusion post the financial crisis, in a big way. But very silently, the central bank of the country has been working very seriously on this agenda. The Lead Bank Scheme, the Service Area Approach, the setting up of CAB, where they started training the bankers, especially in the co-op banking sector as to how to lend, especially to the small borrowers, are examples of the fusion of regulation and developmental banking. By this, they brought the small borrower, who would well have remained outside indirectly into the financial system.

CAB is also working on some projects (designed for MSME borrowers) in a very aggressive way and on building certain technical capabilities which will help in identification of the aptitude of the bankers towards financial inclusion.

M V Tanksale: Any focus programme for financial inclusion which CAB is driving and which can be showcased as a success.

Pramod Kumar Panda:

We are trying to talk more about the soft skills of the bankers and how they should look at the prospective borrowers and how they have to design their products and processes. These bankers would not be cognizant about the standard constraints normally talked about when financing the MSME borrowers.

M V Tanksale: Bangladesh as an example has been quoted since the times of Mohammed Yunus. The efforts in Bangladesh are a culmination of microfinance and financial inclusion. Recently, at a Seminar, the Governor of central bank of Bangladesh drew attention as to how technology is being extensively used in the promotion of financial inclusion. Since BIBM is a capacity building institution, how exactly are two sides - demand and supply, being supported? It is an established fact that unless the demand side is created in a right perspective, the object is not achieved. How exactly was the demand side created in Bangladesh? Have the people started using the facility?

Dr. Shah Md. Ahsan Habib:

Financial Inclusion Strategies - Whenever we talk of financial inclusion, it is mainly about deposit services, finance services and maybe payment services. Carefully observed, we are greatly inspired by these two services - deposit and payment. What about finance services which is almost stagnant? Whether it is Bangladesh, India or anywhere.

Insofar as Bangladesh's financial inclusion strategies are concerned, the strength lies in the fact that the present central bank Governor is personally interested in taking it forward. The positive changes taking place have been greatly enabled by technology. On the demand side, on the payment front, technology has helped a lot – bKash, a payment transfer technique is doing well. We have more than 400,000 bKash agents operating from different corners of Bangladesh.

The customer has to approach the agent, open the account and transfer of funds can then take place from anywhere to anywhere immediately from the mobile. Bangladesh has nearly 110 million mobile subscribers, which is a positive strength. The central bank and other banks have also played a significant role in financial literacy, in awareness development. It is not easy for the rural population to use the products comfortably since literacy rate is low. Technology is also being considered as a part of the green banking initiative. Green banking implies that nobody is excluded. Green banking is part of the inclusive strategy of central bank.

The current green banking policy framework that is followed by all the banks in Bangladesh was prepared at the BIPM campus, in 2011. The outcome has been very good. Online banking is the starting point of green banking, because this saves resources and time. This is at the core of the green banking initiatives of Bangladesh.

M V Tanksale: The model which is in place in Bangladesh - is it driven by MFI or the BC model? Who are the representatives of the banks?

Dr. Shah Md. Ahsan Habib:

MFIs, or as at present even small retailers could be agents of banks.

M V Tanksale: A lot needs to be done in Asia-Pacific to improve inclusion. When we talk of FI, we are clear that we are looking beyond accessibility. Accessibility has been by and large achieved in most of the countries, but we need to go beyond banking accounts, to meet the credit needs, to meet the insurance needs, the pension needs, etc. How exactly these activities have been driven?

Dr. Shah Md. Ahsan Habib

When we talk of credit, interest rate is not the issue, it is about the processing time, documentation, formalities. More than 90% of the banking population is availing credit from the banking sector, but a huge margin of people borrows from money lenders, from the informal sector. Because the loan in the informal sector is given in 10 minutes. Whereas banks and MFIs, have their processing periods, etc.

M V Tanksale: NABARD has been working for several years for removing the people from the clutches of money lenders. Ultimately the brick and mortar branches of the banking industry cannot meet the requirements of the Financial Inclusion. What model should be the right model to ensure that the BCs deliver what is desired/expected of them as a representative of the bank?

H R Dave:

When RBI first came up with the BC Model, a set of guidelines were rolled out stating who could be the BCs. When the banks appointed BCs, the emphasis was on picking up somebody outside the system - corporates and individuals outside the fold, from the kirana shops, medical shops, the petrol pumps - those who were not a part of the delivery system of the financial services. Some entities which were missed out/ overlooked, included the milk cooperatives, the 100,000 co-operative societies and 7.7 million SHGs. These entities were already part of the financial architecture and had they been considered, some of the good Self Help Groups who have been customers for five years, and who are aware of the need for savings and credit and the issues involved, could have helped more in financial inclusion. SHG women appointed as BCs in UP and MP have done very well.

The viability of BCs- Gujarat, where there are very few branches in the tribal areas, is where the intermediation is required. Viability therefore becomes an issue in difficult areas. Again, would banks like to use the network of BCs in promotion of Joint Liability Groups? Training is not an issue, as this can be undertaken by NABARD, IIBF, NIBM or BIRD.

M V Tanksale: Taking the issue of viability further, when we talk of viability, for a person to continue as a BC agent, they must get compensated sufficiently so that they can adopt this as a livelihood or as an employment for an unemployed person. To meet that requirement, the BC has to support the bank to earn that much of a profit from a client relationship. Unless this equation is established, how do we really drive the viability of the BC model?

H R Dave:

NABARD has assured funding of JLGs through BCs in tribal areas. Some banks kept 50% aside for incentivizing the branches for doing extra work and 50% was passed on to the BC. If an individual working as a BC is able to promote 10 JLGs, he/she can earn ₹ 10,000 in a year. Even normal BC operations cannot fetch the BC that much in difficult areas. The challenge is to find what add on can be given to the BC, how do we build a viability model/commercial model which enables the bank to also make profits.

M V Tanksale: We have been talking of the FI being viable. But the challenges of viability still persist. There is no lack of ownership from the Government or the central bank even in India, where these initiatives are concerned. But is Bangladesh doing something different to see that the banks are comfortable in adopting this model which is viable?

Dr. Shah Md. Ahsan Habib

There are several refinancing and interest subsidies facilities. However, not all banks are motivated to perform all these activities. Only the pressure from the central bank pushes them to achieve targets. Each and every bank must distribute 2% of their loan portfolio to the agricultural sector. This is a compulsion from the central bank. At the same time, central bank provides refinance facilities and interest subsidies to ensure targets are being achieved. In a market like Bangladesh where we don't have market incentives, such regulatory incentives are needed to make the push.

Mr. M V Tanksale: Ever since Financial Inclusion was introduced as a concept, in 2005-06, we talk about the poor being bankable, and FI being viable. As a regulator, there is always concern that it should be viable. How can the model be viable commercially and not through the gap funding? The gap funding is not happening adequately, because probably there is a gap in understanding what is the gap. How exactly can it be made commercially viable?

Pramod Kumar Panda:

An interesting issue, a core issue, the crux of the matter. One of the reasons why Financial Inclusion really doesn't succeed is that, both from the business side and the regulatory side, we do not have a hang of what really is happening in terms of the economics. But there is talk of the BCs not being viable or the banks stating that they cannot part with more than they are doing at present. The document which talked of 100 small steps essentially looked at the whole issue from a totally different paradigm. It talked about inclusive finance for the first time from the point of view of competition. Only if people can compete, would they probably succeed. The most important part which needs to be looked at is whether we need to develop capacity and orientation for doing Financial Inclusion operations. It is not the thing everybody can do.

Mr. M V Tanksale: Regulator has recently given licence for MUDRA Ltd., for MSME sector, where we feel there is lot of exclusion especially on the micro side. How will these things really deepen the Financial Inclusion in the country?

Pramod Kumar Panda:

If you look at the data, a significant percentage of the MSME sector stand excluded. Despite the efforts, things have actually not happened. Perhaps one of the reasons is that there is a fundamental structural issue in our banking organizations which are large, mandated and not driven by competition in the substantive sense, which has not seen merit in MSME lending. However, studies have shown that there is lot of wealth to be unlocked. But it is intriguing to find that when it comes to banks operating on the ground, it doesn't get translated into delivery of credit. There is a mismatch between what happens on the ground and what economically sounds intuitive. This mismatch is probably attributable to the fact that people have not spread out truly. Once it is tested out and it is established that there is lot of money to be made, there will be a big push.

The forum was then thrown open to the audience for a Question & Answer session.

M V Tanksale: Any international delegate willing to share the experience of their country is welcome. I would like to hear the experiences from Zambia. How things are shaping up in there and how differently they are handling capacity building issues for Financial Inclusion.

Zambia:

Bank of Zambia has been quite efficient and proactive on the issue of capacity building. We had a situation where banks were failing till the 1990s. But that is no longer happening. It has not happened since 1998 largely due to the efforts put in by the central bank to accommodate the banks. There is very large capital requirement for foreign banks and a much smaller requirement for local banks. Nevertheless, it is still very high. There are 19 commercial banks operating and 30-40 MFIs. Some of the MFIs are lenders to the small marketers, entrepreneurs etc. It is a widespread market also including the leasing companies, merchant banks etc.

Question: The viability issue largely arises because the BC agent does not have sufficient transaction revenue. There is not much demand coming at the touch point. Experience shows that if the BC agent caters to the transactional requirements of the SHGs, this can incrementally add 20-50% of the demand side transaction value, which can make it more remunerative for the agent and thus contributing to the viability. This is currently happening in silos and the BC agent /corporate BC is probably not aware of the SHG model which is the primary point of financial inclusion as rightly pointed out earlier. So convergence at the last mile level is a welcome step and we have seen strong outcomes coming from this experiment.

Last year, RBI had said that cash in the hands of the BC agent is bank's cash and banks should own up that money and place that money from the bank's side as in a normal banking operation at the branch. Not much progress has been seen at the ground level because, it is practically difficult and probably because the risks are high or due to other reasons. More than the financial risk, if this contribution by the Branch Manager is seen as bank's own capital, the relationship would see a shift and the ownership would be far better than what it is today of the BC channel by the branch staff.

M V Tanksale:

Bankers feel that both the models can be effective. It is not a real big issue. The big issue is that we will have to move beyond 'cash in and cash out'. Viability just cannot be achieved only through the transaction module. We will have to go beyond the 'cash in and cash out' where all the requirements of any individual are met. For instance, we now offer products of social security - insurance products at very nominal rates, pension products, micro credit of ₹ 5000 to an individual etc. The Govt. has committed for the entire DBT to be routed through the banking accounts. Cash management at the hands of the BC will have to be the responsibility of the bank because, if the bank cannot really provide a cash out, as is being made available to the individual when he was getting his cash payment for his labour, the routing of DBT will not succeed. Banks will definitely need to take a call to make it more efficient but the viability will have to be looked beyond the transactions. Transactions are important, and we are claiming 182 million accounts being opened. But 42% of these accounts are still having zero balance. The thrust will therefore have to be on the demand side, that is, the literacy angle. This is where organisations like GIZ, Microsave and other stakeholders in the industry will have to work, collaboratively and collectively.

H R Dave:

There are very limited products offered by BCs today. Is it possible to expand the range of products which customers can operate through BCs? Looking at volumes or substantial incentive for the BCs, the range will have to be diversified. There are 13 crore farmers in India, but how many Rupay cards have been issued? How many PoS machines have been installed in rural areas? How many fertilizer depots/ places/vendors are there where the Rupay card can be used? While banks prepare themselves, the PoS machine kind of facilitation needs to be installed where the vendors can use the Rupay cards.

M V Tanksale:

I agree. Rupay Kisan cards have been issued, but there are not enough PoS terminals available – with the fertilizer/ agricultural implements dealer etc. A country having a card base of almost 550 million, including debit and credit cards and there are only 1.1 to 1.2 million PoS terminals. There are roughly around 200,000 ATMs and 200,000 micro ATMs, but acquiring infrastructure vis-a-vis the card base is certainly not enough.

Question: The whole crux of the discussion today has been why the demand for the banking products has not been good. Only one solution for this is the education base. The World Financial Development report 2013 has singled out India for the lack of basic education. This should then lead to the next step of financial literacy. This is a sector, along with infrastructure, health etc., which have been neglected by our development plans. The education expenditure to GDP in India is among the lowest. From the bankers' perspective, why not take the CSR activity together with financial literacy? Branches should be actively involved in the education especially at the primary education pool.

M V Tanksale:

This is a relevant issue and I would like to highlight to the audience and the delegates what the banking sector is doing. It is right that demand can get created only when the education is there – whether it is financial education or formal education. Towards this, the first initiative taken by the Govt., the regulator and the banks is the setting up of the Financial Literacy Centres. Today in the country, in approximately 670 districts, there are more than 1200 FLCs operating, which are manned by retired bankers, who are expected to move around and spread literacy. As an initiative from the banking industry, we have launched and embarked on a scheme called "SchoolBank Champs" scheme where each branch of the bank has adopted one school – there are 120,000 bank branches and thus 120,000 schools will be adopted. This is still in process and is being driven by IBA, with the cooperation of several Govt. departments. Through this, students above the age of 10 will be imparted education in financial literacy. (Incidentally, India is the only country in the world where a minor above the age of 10 can open a bank account, have a debit card and internet banking facility.)

Through this massive programme, trainers training is taking place and teachers will also be trained, with Govt. Support. In each school, one teacher will be identified to drive this programme. Special reading material is also being created for this initiative. The idea is to ensure that they not only become the economic citizens but also that they will be an influencer on the parents. Today, the challenge on the PMJDY accounts is that those who have opened the accounts are not aware of what is to be done next. If the parent is not able to say what is to be done next, the child in the house will be further confused. The first literacy series issued by RBI was on Money Kumar – a child is explaining what money is all about. The idea is to develop the children of the school as economic citizens and through them, we would like to influence the rural population who are not really very literate. In general terms, the literacy level across the board in the country has however improved.

Pramod Kumar Panda:

The initiatives have been taken at different levels:

Women: The focus for some time has been on school and college children. The focus needs to be shifted to women also. Initiatives are also being made not only on literacy but also financial education.

Children: RBI is working with the State Governments, to integrate some educational courses into the curriculum of the children, in schools and colleges where the children understand the basic tenets of finance like time value of money, etc.

Migrant workers: Separate sessions are also being conducted for them in collaboration with international agencies.

Teachers: There is a need to make them more financially educated.

MSMEs: They need to be made financially savvy, understand the typical financial processes, banking processes, different concepts of investments and other things in a simple manner.

M V Tanksale:

IBA is actively involved in this and the resources will soon be introduced in the curriculum at the school level.

Question: The 40% PMJDY accounts which are not funded – is it on account of lack of education or because people do not have the funds to deposit in the account.

M V Tanksale:

That could be a reality when we say that 22% are below the poverty line as indicated by the census. But even this population can deposit nominal sums if they so desire. One day they will be the beneficiaries of all the DBT benefits which will be routed through these accounts. Education is the answer to all issues. It is necessary to create situations where he/she will come forward and do so.

H R Dave:

There is distress in rural India today. Banking system also has a role to play as enlightened institutions. How do you position the output of the FLCCs to address the distress in rural economy? Unless the customer succeeds, the initiatives cannot succeed. There is a case for looking at efficacy of FLCCs while addressing this issue.

M V Tanksale:

I totally agree on this. Like putting various activities on a benchmark, why not put the FLCs also on a benchmark and rank them. This could be explored. Efficacy of the FLC should be ranked and the FLC should also know they are not above scrutiny.

Mr. M V Tanksale thanked the panellists and the audience for an interesting and stimulating session.

BANK QUEST
THEMES FOR NEXT ISSUES

The themes for next issues of "Bank Quest" are identified as:

- July-September, 2016: Stressed Account Management & Financial Stability
- October-December, 2016: Digital Banking
- January-March, 2017:Business Analytics
- April-June, 2017: Challenges in Infrastructure financing

3rd Session: Payment Systems – Evolving Paradigms

Theme presentation: Mr. S. K. Datta, Joint Director, IIBF

Panel: Chair: Shri. S.R.Bansal, Chairman & MD, Corporation Bank.

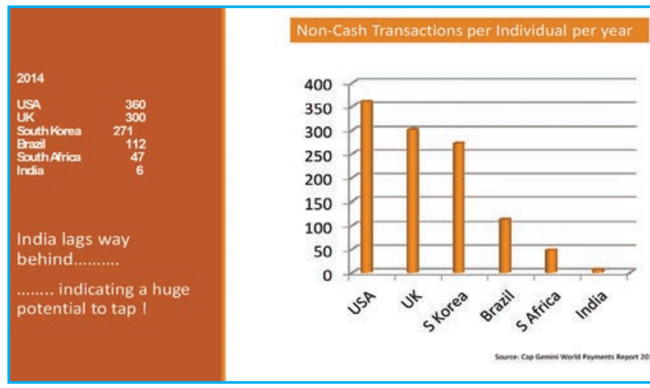
Mr. A.P. Hota, MD & CEO, National Payments Corporation of India.

Dr. A. S. Ramasastri, Director, IDRBT.

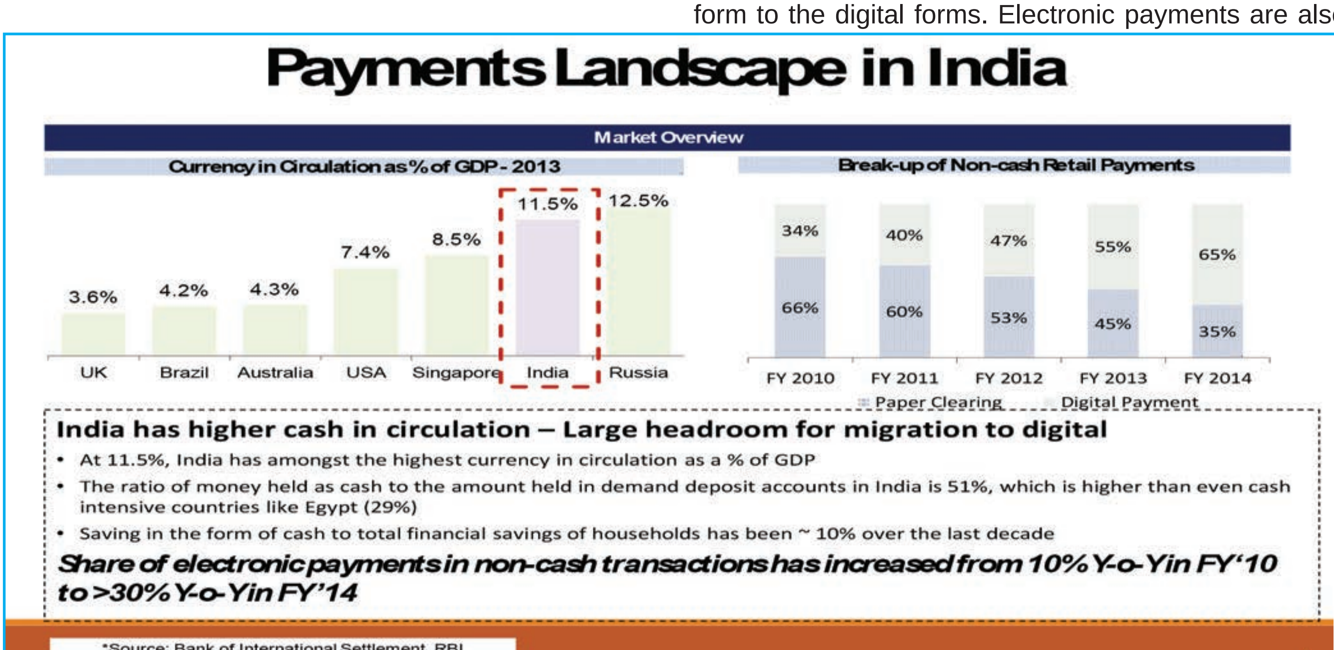
Mr. Shishir Mankad, Senior VP, Axis Bank .

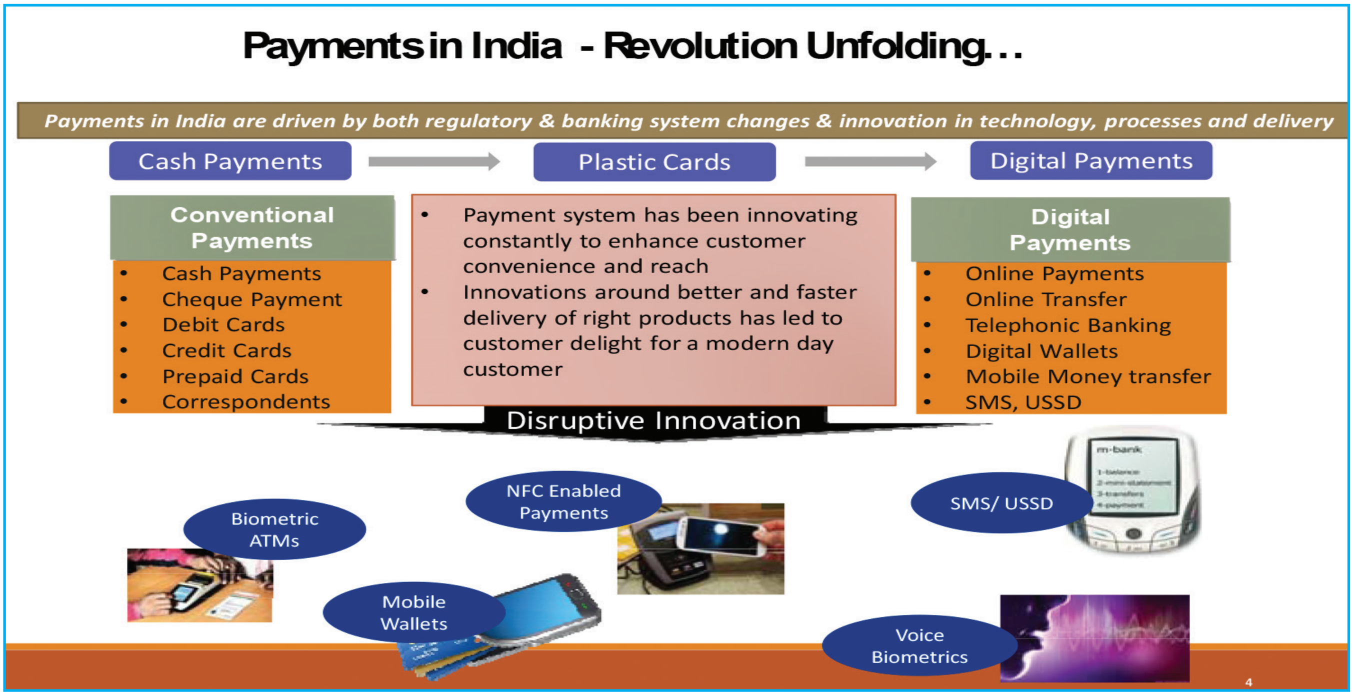
Mr. Sanjib Subba, CEO, National Banking Institute (NBI), Nepal.

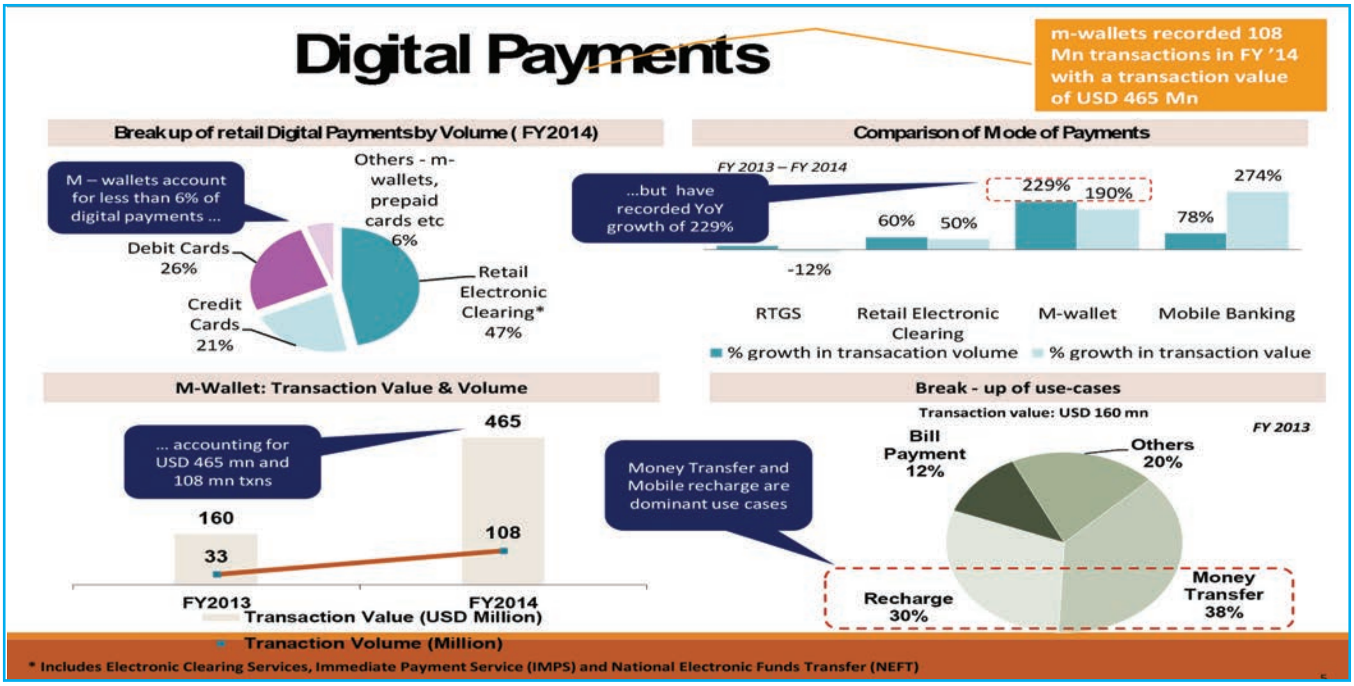
Mr. S. K. Datta introduced the panel members. He highlighted the importance of the theme for speedier financial inclusion.



The amount of cash in India is very high and there is a large headroom available for channelling these savings into the banking fold. There is consequently a large scope for increasing the payments volumes. There has also been a large shift in retail payment from paper form to the digital forms. Electronic payments are also

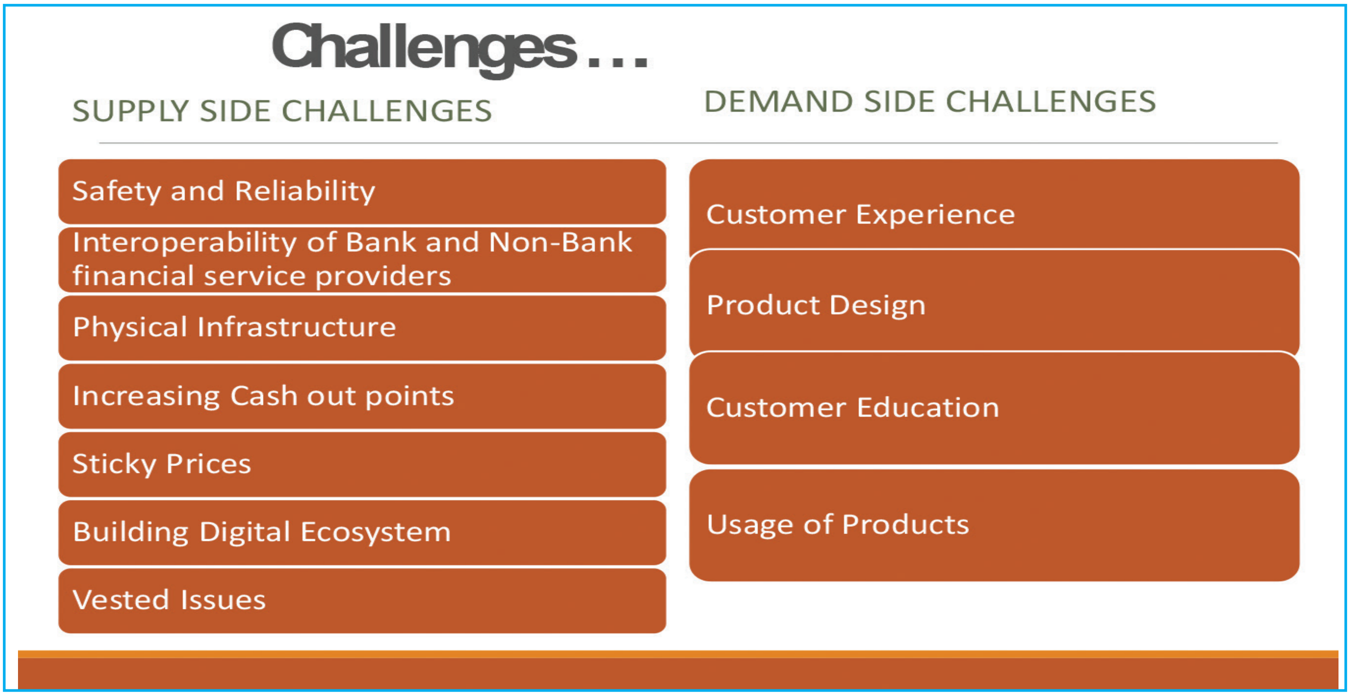






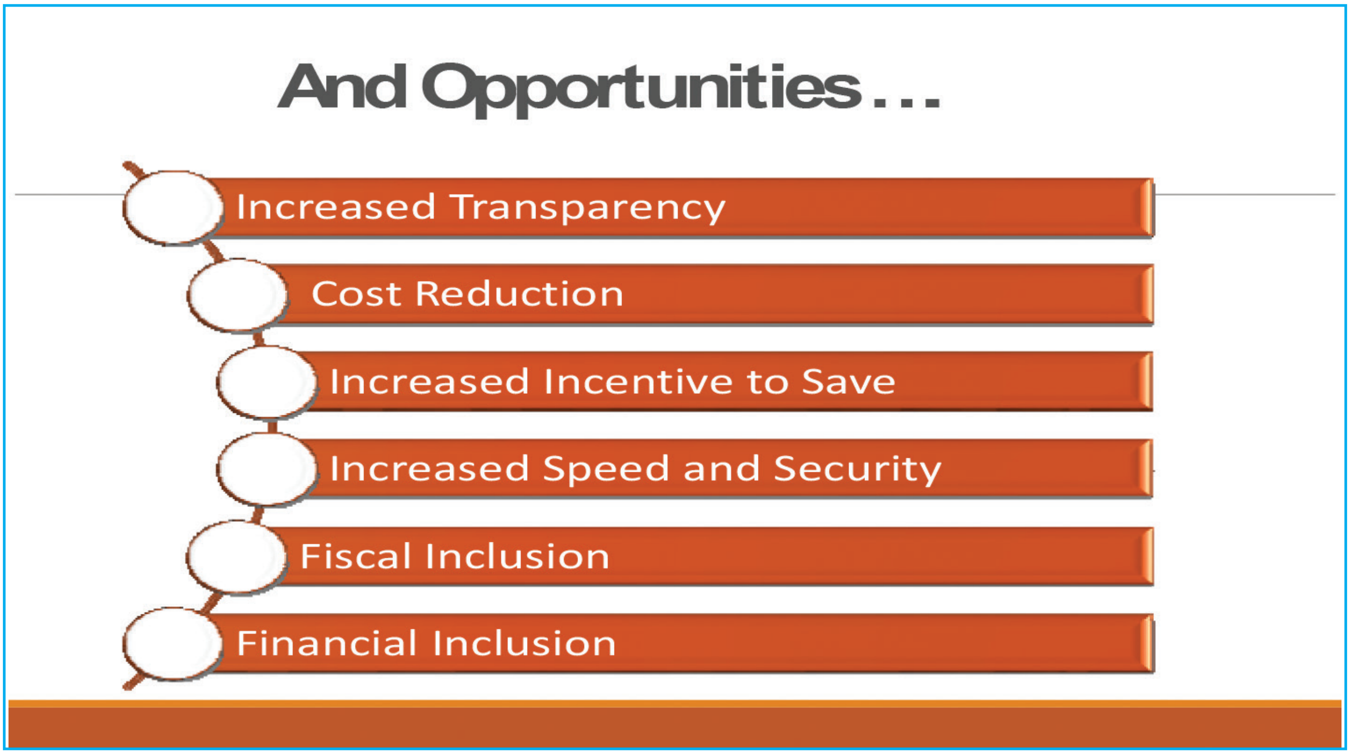
increasing at an increasing pace.

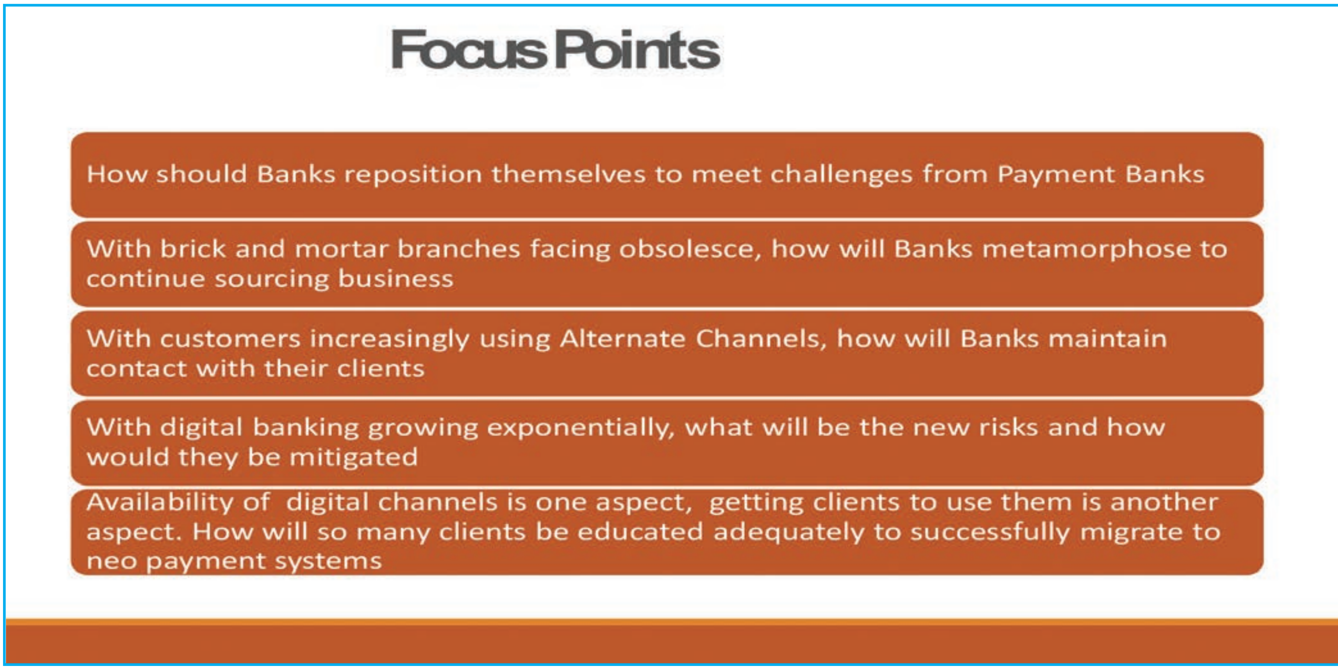
Mr. Datta compared the position in India vis-a-vis the other parts of the world. He said that there is a huge scope for electronic transactions. In UK and USA, the no. of non-cash payments per person per year is around 300-360, in India it is just about 6 in India and China.



Mr. Datta described the evolution of the payment systems in India, over the years. He also touched upon the disruptive innovations introduced in recent years.

Mr. Datta emphasised that it is the wallets which has shown sharp exponential growth both in volumes and amounts.





He also listed out the challenges faced by the banking sector both on the demand and supply side.

But, he stressed that there are huge opportunities, which includes not only financial inclusion but also fiscal inclusion, for the banking industry which should be properly tapped.

Mr. Datta finally listed the focus points which may be the basis for discussions by the panel.

Mr. S.R.Bansal then set the panel discussion in motion.

S.R.Bansal:

The payment mechanism to bring in more efficiency and transparency in the system is moving from cash to contact less payment to mobile money in India. This evolution has been made possible consequent to a series of measures initiated to contain the systematic risk in Payment & Settlement System. Besides the regulatory push, the Government initiatives such as JAN DHAN YOJANA, DBT, etc. have further given a big fillip to this shift. The emphasis on digital India would further intensify the movement helping to cover more and more numbers of entities and people bringing in speed and ease of making payments. It is in the last 10 years that India has witnessed this major shift from cash based payment to electronic payment system. This was mainly due to various measures taken by Government of India (GOI) and RBI, including introduction of Payment & Settlement Act, the setting up of RTGS and NEFT and of National Payment Corporation of India (NPCI), regulation and promotion of alternate channels and payment gateway and guidelines or security measures for the electronic transactions. This shift has also been increasingly aided by evolution of telecommunication and computing technology, both in terms of speed and reduced costs. While electronic payment system has registered impressive growth, the benefits of the modern electronic payment system are yet to reach many. They are generally now limited to the tier 1 and tier 2 locations. So, the benefit has been limited to those citizens who already have access to formal banking.

The financial inclusion efforts by the GOI in the last few months, have helped in gathering speed in reaching out to the villages. The Aadhar infrastructure has given a significant support to these efforts. Today, we are seeing a transformation of the payment ecosystem not only in retail segments but in all segments such as b2c, b2b, Govt. to citizens and consumers to Govt. At 11.5%, India has almost the highest currency in circulation as a percentage of GDP. This leaves much room for migration from cash, cheque to e-payments. Non cash transactions per individual are very less. 6 per individual per year as compared to 360 in USA and 300 in UK. Payment through m-wallet and prepaid instruments is less than 6% of the total digital transactions. Also, the population using internet through mobile is expected to touch around 70 crores by 2020 as compared to the current level of 26 crores. It is estimated that internet banking users will grow from the present status of 6 crores to 23 crores by 2020. This type of scenario has posed great challenge to conventional banks to reorient and to reinvent products and processes which have the capabilities to face the challenges of the emerging customer preferences and to retain its prominence in the financial world.

All these developments show the remarkable changes happening in the payment sector, but it is a fact that only those innovations which offer a combination of consumer benefits by way of convenience, speed, reduced cost and error free settlements would only survive. The entry of new payment banks and new players will definitely increase the competition in the industry. It is evident to all of us that, those who have got the in-principle for payment banks have platforms for assessing the customer base, have infrastructure, expertise, technology and also adequate capital base. We must prepare ourselves, to take on these challenges and to be more innovative so that we not only match the products and services that are on the offering from the new players but also meet the growing requirements of the customers. Banks may also explore possibility of tie-ups with these entities so that it can be a win-win situation.

S R Bansal invited the panel members to share their thoughts on how banks should position themselves to meet the challenges from payment banks.

A.P. Hota:

I would like to elaborate on the payment system in India, for the benefit of the international delegates. During the last 10 years, the payment landscape in India has undergone a metamorphosis. All possible advanced payment systems that can be thought of are available in India now. The traditional mode of clearing has also been modernised in the form of cheque truncation system. The older ways of salary, dividend and pension has come to a new platform- the ACH. Mobile banking has come up in a big way. Although the number has not picked up, it has been put in place. The country has developed a card brand of its own. All the 200,000+ ATMs have been made interactive. The number of PoS terminals is impressive, but not good enough. E-commerce has gone up in a big way almost 30-35% increase YoY growth and the indications are that it will grow significantly. Although many changes have taken place, there are a lot of things to do.

It is in the wisdom of RBI that new set of institutions which are focused on payments, dedicated for payments, should be there to further two purpose – financial inclusion and innovations in payments. Obviously, the first response of the banks will be – what is that was lacking that the payment banks have now come? Payment banks will have a few disruptive innovations. Some of the new payment banks are coming with a card payment acquiring business which is totally different from the traditional ones. They are coming out with PoS terminals which can be discarded if they are defective – low value, low amount. Banks so far have not gone for that. So the first response is whether to compete with them or co-operate with them. Of the 11 new players, there are 3-4 players who have tied up with the banks, which is a good move. For instance, SBI- Reliance. Reliance is thinking of installing 2 million PoS terminals.

The telecom companies and the banks have been having differences on which convergence could not be arrived yet. Now they are coming to the banking stream and they would be part of the banking infrastructure and the USSD infrastructure. They were running the USSD and now will be part of the banking system. It is good that they are now coming as payment banks and with banks accepting them, the interoperability would be at all levels. Now USSD is interoperable, but interoperable to the advantage of the telecom companies' and to the disadvantage of banks. Once the telecom companies become banks, possibly things would be different. They have a direct connect with the customers by having large outlets. They can access deposit faster. It is a good thing for the country, for the customers, and banks if they can leverage. Banks need not see them as competitors but as partners. In their mandate, they can act as the BCs of other banks. So why not utilise the mandate instead of competing.

RBI's vision to bring the new set of institutions is to fill the gap and to meet the need for bringing innovations in the payment system. An example of disruptive innovation – When WhatsApp replaced the SMS – similarly in the payment space, if a new player has the WhatsApp attitude, atleast, the micro payments can be brought to the table by the new banks. This will be good for the customer and the country. Banks should leverage and not look upon them as competitors. Way back in 1996-97 the PSBs had thought that with the entry of Private Sector Banks, the business would be eroded. This however did not happen. PSBs have really prospered along with the growth of the Pvt. Sector. Now the payment banks- the initial perception would be a threat and if they can really work out /respond to it in a positive framework, it would be a win-win situation for both.

S. R. Bansal: So many disruptions coming in, it is not a threat or competition but a partnership.

A. S. Ramasastri:

Traditionally, we understand banks which take deposits to lend. But the main focus of the payment banks is not lending; they are not expected to lend. They will be occupying the other space, i.e., payments. Traditionally, most of the payments were either cash based or non-cash based. All non-cash based payments were routed through the banks. So, banks came more and more into the payment space. Once the payment space came to the banks, they were expected to give more features to the customers so that they will be able to do the transactions more comfortably. Three important features that a customer looks for – cost, convenience, control over the transaction at any point of time. Banks were expected to do this and have been doing it quite well.

During the last 4-5 years, different kinds of payment systems came to be introduced. We started with RBI setting up the RTGS, NEFT, etc. but they were central bank managed. Slowly, the movement has moved from a central bank managing the payment system to various private parties and others. It is happening across the globe. When the payment systems across the globe were studied, in the developed countries, the private parties were driving the payments including on the digital platforms. In other countries like Kenya, it is not the private sector but the entire ecosystem that drove the need for change. In India, it is neither the model of the developed countries nor the model of the other countries like Kenya. Banks were therefore, not able to enter the space fully. Digital wallets and other things are being introduced but these have limited usages. It is in this context that RBI thought that It might be right to come up with a system of banks which will be exclusively devoting themselves to payments. What are the challenges that the banks might face when these payment banks come?

- because of their reach, they can collect deposits also, is there a challenge to existing commercial banks – deposits which they were earlier enjoying is possibly going to go to payment banks.

- most of the payments that the merchant banks and others are doing is going to move to the payment banks and most of it is going to be managed by them.

This is a challenge. Because the payment banks are those which already have the kind of technology that is required to provide low cost high convenience and lot of control over the system. Mobile penetration is very high in India. Mobile companies - are they in a better position to provide this payment mechanism? Another thing is postal officials, who have a good reach across places, especially in villages where they are friendly with the locals, whether they will be able to come and deliver the services, which are actually required for the people? This is another challenge the banks may have.

But what are the challenges to the payment banks? Looking at the whole space, despite the efforts of the regulator, Govt. and the banks, why did we not take steps to encourage people to participate in the technology payments. It has not happened. When the new banks come, they also have to address this issue and identify the gaps. The major issues identified have been lack of awareness, lack of education, both formal and informal by the bank staff. Most important is the trust. Encouraging people to use the new technology and ensuring them that the systems are safe is going to be the immediate priority. Are the people going to believe that if they send a transaction through this mechanism, it will work? How will their trust be built in the system? If they are able to bring them into the fold then it will be a good thing, because more people will come into the banking fold using the payment space and the new products and certainly the banks will also take advantage and the whole combination will work for the country as a whole.

The next 2-3 years when the payment banks begin operations will be an exciting period for the country and we have to see how the payment scenario will undergo a complete change in the country. Also disruptive technologies are good but are they good for a country like India where we are spread out. Having diverse participants may not always help disruptive technologies.

S R Bansal: There are two things –

- there may be threat for deposits, but through JAN DHAN YOJANA, we have experience of reaching out to the rural masses and creating faith. We have also shown that JAN DHAN YOJANA is profitable. The BCs are working and if we make them more active, we can meet the challenge of the deposits going away and

- cash will be replaced by non-cash and therefore, banks will have more space to do some more business.

Shishir Mankad:

In Wells Fargo, Chicago, they talk of the history of Wells Fargo – how they started as a carriage business – logistics company carrying mails from place A to place B and that mail became a bill and that bill became money and Wells Fargo became a bank. That Wells Fargo of 200 years ago is unrecognisable from the Wells Fargo of today, which is a very technology intensive, very astute, very diversified institution. Much the same degree of transformation is looming large upon the Indian banking system and for good reason too.

There are two ways at which banks can look at with payment banks coming in – the first response is agility. Conceptually, payment bank is a focused business on primarily one line of activity which is payments and therefore, banks which are a conglomerate of financial business, have to compete against this focused nimble player. So, the first response should be agility. Banks will have to decompose the banking business as seen in the digital part of the banking business. Banks have to figure out how to become agile. While the payment banks will have wallets, the unsung fact is that massive growth in mobile apps has been seen at the banks. We are seeing a revolution within today's banking systems. The challenge for banks is going to be how we create the internal framework to allow for that agility to foster and grow so that we can take the payment banks head on. That is a competitive way of responding to the issue. Another way is back to basics strategy. Fundamentally, banks provide the five financial needs of the consumer – save, invest, borrow, Insure and transact. Banks should think very carefully about where their real competencies lie, what are those things that differentiate them from the payment banks, and build/augment business on those lines. This is a very fitting response strategy. If the two are put together – agility and back to basics – it comes to a situation where, in some places banks will compete and in some other places, they will collaborate. In short, it can lead to co-opetition (co-operative competition). We will need to figure out where we will compete with them, compete hard and build the capabilities. But there are enough places to collaborate and we can feed off the innovation and the markets that they open. Basically, banking is a flow business and the more the flows that are created and the bigger networks that are set up, everybody in the system benefits. We need to figure out what are the spaces that will get opened up when the payment banks come and feed off them. We need to think why inspite of so much intervention, we still regret and lament on the relative progress of financial inclusion. It comes down to the basics that the bank is supposed to offer, trust, reliability, convenience, fairness, etc. The basic tenets still remain and banks, payment banks, network institutions need to sit and solve for financial inclusion to take off. The question why the customer is not using the pre-existing infrastructure still remains centre stage.

Sanjib Subba:

I would like to share some perspective from Nepal – what we are experimenting with branchless banking, in terms of leveraging technology when it comes to banking. Nepal banking landscape is very new. The private banking has a 30 years' history but a large chunk of the private banking has been around only in the last 10-15 years. Nepal went directly to CBS system. Most of the Nepali bankers have not worked in the manual system unlike their Indian counterparts. It is an advantage, but the size of our banks is small. The largest bank in Nepal has not more than 150 branches and 100+ ATMs. The country total is 1650 ATMs. But the banking industry has not looked at the ATMs as sales and considers the ATM as a value added product. Per day transaction hit has to be atleast 275-280 to break even for an ATM. No ATM gives a break even in Nepal even from the ROI perspective. The gap between the debit card and total deposit accounts is almost 8 million. Against 13 million deposit accounts, 4 million debit cards have been issued.

There is a lot of customer orientation, education and cross-selling skills of the lower level and frontline staff has to be carried out at a large scale to address the issues. In the last 4-5 years, we started experimenting with branchless banking and online banking and even mobile banking without much success. People still prefer brick and mortar, they would like to come to branches and there has not been much success. The no. of branchless banking transactions works out to one transaction per customer in a year, which is very low.

In Nepal, the currency in circulation is around 16% of the GDP. The society likes to feel the cash and is not comfortable with plastic money. Access to finance – we should re-term as access to form of finance. From my perspective, there is a huge difference. Our markets in the emerging markets are informal and challenge is to bring in this informal financing to the formal financing sector. In terms of disruptive technology, going forward, in payment systems, be it RTGS etc., the transitions will be fast and quick. The young generation in Nepal is technically savvy. The big question is will we have the bank in this structure in 20-30 years, what is the disruptive technology that will come and compel the bank to change the structure? Will the bank convert to payment banks or will the telco's using the smartphone, by bringing the cost down, be able to take away a large chunk of the bank's overhead? The technology investment by telco's- will it help balance the spread? Will it reduce the cost of funds?

S R Bansal: You have the advantage of directly being on the CBS platform and techno savvy young country. There are not much barriers for your country.

Whenever I travel, even in smaller villages I find Axis Bank. They have been able to penetrate into rural India and into areas where others fear to tread. With brick and mortar branches facing obsolescence, how will the banks metamorphose to continue sourcing business and also with customers' increasingly using alternative delivery channels, how will banks maintain contact with the clients?

Shishir Mankad

Axis Bank sees a long time ahead for the brick and mortar branch and do not foresee branch's obsolescence. Fundamentally, that is the assumption we are making. It is accepted that the role of the branch is changing and changing rapidly and putting lot of demands on the bankers to figure out what is to be done. But the branches are an integral part of the Axis Bank's offering to our customers' – be it retail, corporate or Govt. What changes are we seeing in the work profile as we go forward. Clearly, routine transactions are plateauing even reducing in some urban areas. There are three roles for branches –

1. Advisory- customers still need to come to banks for advice. There are moments of truth where they have to make large decisions, maybe mortgage, investment, large deposit, insurance. For large decisions, they need some advice and branches are well positioned to deliver on this front. There are remote channels where this can be delivered but branches have an important role to play in this and it will likely continue to be so.

2. Issue resolution- customers sometimes have issues to be solved and there again, the branches will continue to have a big role to play.

3. Accelerating and evangelising the digital channels.

Axis bank has 1500 cash deposit machines which are self-service devices for customers to deposit cash. Almost like a teller. Initially, customers were hesitant to use the machines, and obviously they needed assistance to use them. For some time, assisted models to help customers to move to digital platforms will be an important part of the branch model. This is not new. Even when the ATMs were introduced, the bankers had to assist the customers in the operation of the card in an ATM machine.

The size of the branches is however coming down, since the work culture is changing and we are evolving the model continuously.

How do banks maintain contact with their clients in the digital world – digitally. But how is it to be done?

1. To integrate contact-ability as a fundamental part of on-boarding. A challenge is integrating contact-ability has legacy issues. Keeping pace with the change

of address, mobile phone nos., is a challenge. No requirement for customers to update this info with the branches. Bank is trying to integrate contact-ability in every transaction, every account opening, every on-boarding. Some of these are needed for OTP, etc. But fundamentally, the contact-ability is needed to on-board a customer to a transaction. This ensures that bank is in touch with the customer.

2- With lot of data infrastructure coming into the picture, a Pan card is not necessary. Only the number is required, which can then validate data from the NSDL sites. CIBIL has got good coverage. Social media has good uses, particularly for lending. Looking at ways to contact customers on digital social media channel or using data infrastructure is also a big step forward. Banks have started doing this and can do a lot more in this direction.

3- The digital model allows the flexibility to segment the customer much better. Where there is a commercial opportunity at the higher end, personal and physical contact will still be reached out. At the other end, where there is risk perceived, banks may try to reach out in such cases too. These are easier in a digital world.

S R Bansal: In a country like India, the brick and mortar branches may not go away in the near future. In digital banking, in a country like India, where the majority is in rural areas, faith is very important. To create faith, we have to see that risks associated are mitigated. IDRBT are doing a lot of things in this area. With digital banking growing exponentially, what will be the new risks and how will they be mitigated?

A S Ramasastri:

The customer looks for cost, convenience, control, confidence. Confidence/trust comes out of the security which is there in the overall system especially in the case of banking, because money is involved in that. Today, people still have trust in the bank and deposit money in banks. In fact, the whole thing (money) is in digital form. So, comfort level has been achieved. When we talk of payments, and banking though a gadget available with him, either mobile banking or internet banking – the customer has still not developed the confidence. This confidence can come if the banks are able to build a system and convince the customer that these systems are safe and secure. How to convince the customer? How to build a secure system? When the entire IT system is within the premises, in the control of the bank, what are being used are gadgets, which are not meant for this secured system – internet and mobiles – the primary uses of these systems were something different. But we are using them for banking now. This bridging is difficult. On one side, banks have to work at building a secure system and secondly, convince people that the systems are secure.

The issues are slightly different – I get confidence in a system if I keep doing transactions and I don't find much of a problem after I do it for a fairly long period. It is only then that confidence comes or I am very sure that redressal mechanism is exceedingly good – if a transaction is not taking place, I get redressal very fast and the right kind of redressal. If these are to happen, the entire ecosystem should know about this. Today's problem is that the bank staff does not know the digital banking system. If at all a fraud/crime takes place in the digital banking channel, do we have an ecosystem which is legal to address the system and give redressal to the customer. This is also not clear in today's circumstances.

By building these digital systems, i.e., the anytime anywhere banking, adequate security needs to be built into it, ensure that it is monitored and ensure that it is working well and if something goes wrong, there are people with adequate knowledge to understand and bring it back to normalcy. Institutes should focus on security and its importance – security labs, mobile security labs which actually looks into these apps and are able to say whether the systems are reasonably safe. But there are many more things which have to be done for digital banking to succeed.

When we talk of payment systems, we should be able to distinguish between high end systems which are large value, systemically important and where the security levels are very high. But when it comes to customer convenience, there cannot be too much security, but there should be adequate controls to ensure that the losses are minimised and also that reversals are possible in case of losses. So if the system is to be convenient, it cannot be too strong. And if the system is not strong, trust is not possible to be built. So we have to try for affordable security solutions on small gadgets like mobiles, internet, etc. Many of the features are built in but the message should go that they are reasonably secure.

From the angle of technology and risk, it is scary and should be taken care of by the IT team and the banks and not the customers. Customer should have the awareness only. The internal strengths have to be really good. Those who are using the system should be given adequate comfort that the systems are working well.

S R Bansal: All systems are highly secure only that it should be continuously monitored. In India, the number of mobiles is more than the population excluding children and senior citizens. How important is mobile payment in the years ahead? When we see rural India, there is a lot of requirement for education/literacy. So how do we avail the digital channels and get clients to use them? How will so many clients be educated and successfully migrate to the new payment systems?

A P Hota:

Mobile payment is going to play a very significant role in future. Even in the western world, mobile banking is not very popular. We talk of Kenya, Bangladesh, Afghanistan- few countries where it has been extremely popular and they have become very dominant systems in the payments area. In India, it started in 2010 and when it started, it started with a system of immediate money transfer, instant payment from any mobile no. to any mobile no. which is tagged to the bank account. Mobile banking over the last 4-4 ½ years has undergone significant changes.

Inspite of the efforts of the regulator, the banks and the Govt., compared to the premise that we have that 900 million phones and active phones in the range of 650 million, the no. of transaction is hardly around 35 million. It is not significant in terms of numbers but significant in terms of policy that we as a country are growing at 8%. If it continues for a few years, if the e-commerce continues, if the economy grows in all aspects, the kind of transactions that would happen would be phenomenal. Would it all happen in cash? Would we continue to pay 85% of the bills by cash? Would we continue to pay all the shopping experience by cash? Would the banking system be able to handle so much of cash? Even at small places, the demand for cash deposit machines is growing – depositing the cash at the bank in a small town is still a challenge.

Handling of cash would be a challenge for the banks, would be a challenge for the regulator. Here, we are talking of cash to GDP of 11%. If the growth rate goes up, the kind of cash generated would be phenomenal. So we have to move to non-cash system. Which is the most non-cash system that we can think of? Which is the low cost non-cash electronic payment system? It is mobile. That is why mobile has to be the focus. After the Jan Dhan Yojana, the JAM (Jan Aadhar Mobile) has come - how the three can be combined – Aadhar as the authentication, mobile as the device, and the account holders. All the prepaid users have opted for the wallets and the success of the wallets has been driven by the large discounts offered for the users. That is not sustainable. The sustainable method is one which will drive on its own. Mobile has to be made popular.

There has to be a delicate balance between security and convenience. So far, convenience is the issue. The mobile payment system in India is secure enough. It is so secure that people are not transacting. Of 85 banks and 11 PPIs, only 9 banks are doing SMS based financial transactions, because of the fear. This fear has to go. RBI has already relaxed the two factor authentication for EMV based card payment transactions. Atleast, we should consider if the m-pin can be waived for a low value transaction? Say ₹ 200.00 for payments at the local grocers. If the payments are made by SMS, how can it be made simple and convenient? The best solution is contact-less. Contactless – the work is on, but till then, the SMS based system without a pin transaction is also required. Data driven security and analytics driven authentication- instead of every time asking for the pin, can at the back end, an analytics be generated/ transaction stopped - something needs to worked out.

The programmes of the telecom companies should be more user friendly. More secure platforms have to come and that only can revolutionise payments. Also, the interchange and the aspects of interchange have to be addressed. If the mobile banking transactions goes the way of the traditional card based interchange, it will not work. Currently, mobile based merchant payments are equivalent to card interchange. Which is why mobile based merchant payments have not started.

Financial literacy: without literacy all the good things that are being discussed cannot happen and it is possible if it is taken up on a war footing. Literacy should not only be for the people, but also for the bankers and stakeholders. A drive similar to the efforts taken to open accounts is absolutely necessary for literacy, so that people are made more aware.

S R Bansal: Fear has to go and faith has to be created. What is the average transactions in ATMs in Nepal?

Sanjib Subba:

Average hits range from 60-150 per day. As banks and regulators, we should focus particularly that the payment system is at the BoP model – base of the pyramid, i.e., where the large chunks of the volumes are taking place day in and day out. The Government payments and collections, pensions and provident funds which comprise a huge portion of the fiscal channel, if that can be through digital channels, it will take care of the non-cash. In Nepal, it is still in discussion stage and has not yet been formalised. This is a transitional economy and transitional process and bankers will have to really gear up in their risk assessment process.

The forum was then thrown open to the audience for a Question & Answer session.

Question: An interesting point was SMS based banking where we can have a pre-set limit. Whether we can create a database of pre allowed people where the initial due diligence takes place and all are registered and set limits. For these people, these kind of transactions can be allowed. That will free up a huge area. Once the due diligence is done on a small base, in one–two years' time, the numbers will grow.

A P Hota

It is worth trying out. Meanwhile NPCI and banks are working on a unified payments interface. In this, we are trying to simplify certain things which may be for relatively larger values also. In the card payment system, the card is what one owns and what one knows is the four-digit pin. Now we are working out whether we can do two factor authentication at a single click. In a mobile transaction, if the mobile as a device, is authenticated as a onetime measure and if subsequent transactions are done at a click, especially low value payments; authentication may be required only for higher value payments. This is an experimentation which is being carried out under the guidance of Mr. Nandan Nilekani, Innovation Advisor for payments. We also experimented with USSD in bKash in Bangladesh – 4 million transactions a day. In our interbank system, we generate hardly 1 million a day on the USSD platform. Why has it succeeded there and not succeeded here? Some restrictions were imposed by the telecom companies on the banking system and it has also been indicated to TRAI. Hopefully, the issues will be sorted out in the next few months and we will be able to move on the USSD platform.

Question: You mentioned about making the small payments to the local grocer, washer man, vegetable vendor can be made through electronic means. We tried to do this using buddy and the challenge faced – the payer and the receiver both need to have the data connection on their mobile phones which entails a cost.

2nd- since the communication happens through the internet, there are two levels of communication – at the authentication stage and payment stage - and depending on the reliability and availability of the communication; it takes its own time. Every transaction takes between three to five minutes to perform. Nobody is going to wait for that long, especially for small value transactions. Compare that to making that same payment in cash. The whole transaction is over in 30 seconds. NFC as a local means of communication is going to take time. Can we think of other means of communication? One means of communication could be SMS, which again entails a cost. Can we use Bluetooth which is available on all the devices? But for that the payment applications need to be interoperable. And for all payment operations to be interoperable, it is necessary that the payment operations should be sponsored by a national agency like NPCI.

A P Hota:

Making payment across may be easy but the best mechanism is contact less. Contact less takes away the technology from the person. It is the way to go and we have to find how we can do it. Contactless technology is already available with visa and master card. For a large country to move forward, it is ideal to have our own national contact less platform. The national common mobility card which has recently come into play is an example. This can transform the face to face ordinary payments. The speed has to match the agility displayed by the grocer in accepting cash. An equivalent of cash has to be brought in electronic form.

Question: Referring to the World Bank report on migration and remittances, there is a lot of internal migration within the country in India. Internal migrants transfer money but there is no data on that. Is NPCI tracking that?

A P Hota:

An interesting study was conducted by NABARD and GIZ, regarding remittance corridor in India. Another challenge to the bankers - an RRB in a village which is doing very well, but money cannot be sent to the bank directly. Can the RRB be brought under IMPS? How to enable all the RRBs' and all the Co-operative banks on the IMPS platform? If the banks do not respond to this, the payment banks will take away this business too.

Mr. S R Bansal thanked the panellists and the audience for an interesting and stimulating session.

Implications of 'disruptions' – 'Blockchain' technology

The initial concerns over the emergence of virtual currency schemes (digital currencies like Bitcoin) had been about larger issues related to the underlying design and incentive-structures of such privately-owned, internet-enabled alternative currency systems and their implications for the traditional monetary system. Even as opinions diverged on their merits, episodes of excessive volatility in their value and the failure of some virtual currency exchanges proved to be a dampener to their take-off. On the other hand, their anonymous nature that goes against global money laundering rules rendered their very existence questionable. While these issues along with challenges for consumer protection and taxation related aspects are being debated, the key technical concept of 'blockchain' which underpins such crypto-currency systems, is drawing more attention now. With its potential to fight counterfeiting, the 'blockchain' is likely to bring about a major transformation in the functioning of financial markets, collateral identification (land records for instance) and payments system.

The traditional (and presently used) system works on the basis of 'trust' and the 'regulatory' and 'controlling' power of 'central' entities / counter parties. As against this, the 'blockchain' technology is based on a shared, secured and public ledger system, which is not controlled by any single ('central') user and is maintained collectively by all the users / participants in the system based on a set of generally agreed and strictly applied rules. Thus, the 'blockchain' technology facilitates transactions / collaborations among participants / entities which have no information about or confidence in each other, without necessarily having to resort to a neutral and trusted 'central' counterparty. While the notion of shared and technologically secured public ledgers raises the prospects of revolutionising financial systems, the full potential as also implications of its applications are still not known.

At the same time, regulators and authorities need to keep pace with developments as many of the world's largest banks are said to be supporting a joint effort for setting up of 'private blockchain' and building an industry-wide platform for standardising the use of the technology, which has the potential to transform the functioning of the back offices of banks, increase the speed and cost efficiency in payment systems and trade finance.

Source : Financial Stability Report, Issue No. 12, Reserve Bank India, December 2015

Learnings from the conference

1. Globalization, rapid strides in Information Technology and increased expectations of the customers have forced banks to make alterations in systems, processes, strategies and evolve newer products/ services mainly technology driven products on a continuous basis. With the banking sector becoming increasingly complex, competitive and customer oriented, banks have started exploring and experimenting newer business models to meet the increasing challenges not only in India but also in the Asia Pacific region.
2. Financial inclusion is another area where a lot of emphasis is being placed today, with PMJDY. In order to achieve this, currently multiple models like SHG-Bank Linkage, MFI lending, BC models, small banks, payment banks, etc. are operating or will be in operation. However, there is still a long distance to traverse. The capacity building of BCs, the financial literacy of the unbanked, synergising the efforts of the different stakeholders are all important issues. A survey of bankers revealed that identification of the unbanked and penetration of FLCs to the bottom level were imperative for the success of the Financial Inclusion campaigns. The recent campaign aimed at school children were a positive initiative to speed up the financial literacy programmes.
3. The changing banking landscape with the entry of small banks and payment banks would mean that there would be more players in the industry. On the one hand, this would threaten the position of the existing players at least in the medium term. But on the other hand, there will be pressure on the existing banks to innovate. Partnership and collaboration rather than competition will be the way forward. However, payment banks cannot solely substitute the present bank structure especially in the rural and semi urban space, where Public Sector Banks enjoy more trust.
4. The brick and mortar branch as seen today may undergo transformations keeping in mind the changes in the landscape. They may not disappear entirely, but may need to change their focus and core activities. They could well become customer learning centres, delivery points for e-commerce or centres for cross selling of products.
5. It is also necessary to recognise and acknowledge the new paradigms in payment systems which is taking place at a break neck speed. The last 10 years has seen a major shift in India, from cash based systems to electronic payment systems, thanks to the various measures initiated, setting up of the digital platforms, regulation and promotion of alternate channels and payment gateways and guidelines to the security measures that have been put in place.
6. The growing ease and convenience of new and emerging payment systems allowing anytime, anywhere payments is tempting to both consumers and the merchants' ecosystem. With every major telecom player coming into the payment space, the dominance of the banking structure in the payment system is also expected to reduce. The reasons for the shift in paradigm has been varied and has arisen on account of increasing customer expectation, fillip provided by technological advancements and the sea change in delivery procedures.
7. Ultimately, the customer is the king. The customer will always choose the channel and cannot be forced to accept the channel. Not only should banks be geared to deliver in the days to come, but they should also be customer centric. Challenges towards this on the staff front will have to be addressed.
8. The key for banks going forward is of course cost containment, revenue maximisation by improving productivity and also increasing the third party/fee income. The emerging focus areas are risk management, compliance, IT, business analytics, financial inclusion etc. There are also a lot of security concerns with the growing use of Information Technology. Security considerations and confidentiality of data make it necessary for banks to be very careful of the entire system and ensure that there is no data leakage or compromise on the security aspect.

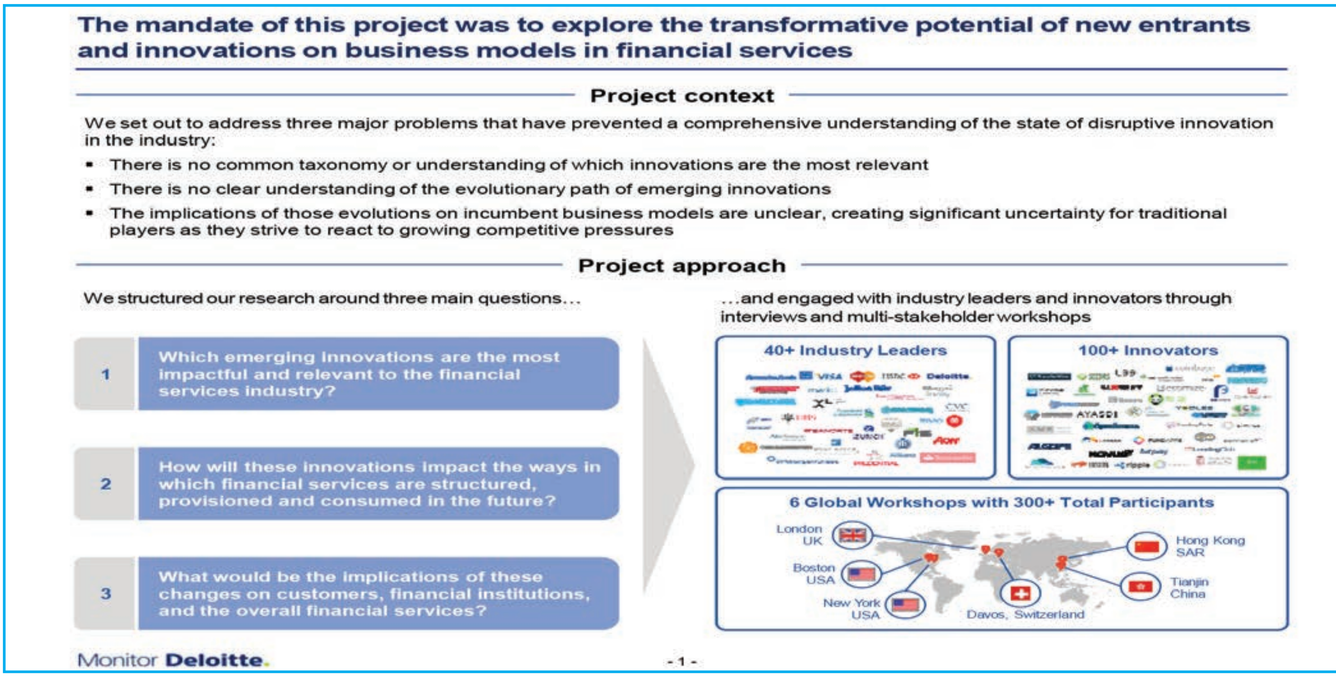
"The Future of Financial Services: How Disruptive Innovations are Reshaping the way Financial Services are Structured, Provisioned and Consumed"

Mr. Chris Harvey*

It is a great honour and privilege for me to be here and to give you a short and interesting talk. Mostly, it will stimulate some discussions and at the end of the talk, we will have a Question and Answer session. The Q&A will stimulate some debate. There are no right or wrong answers to the idea but I will deal on what is happening to our industry and where actually it is going.

Everybody knows about the 2002 dot-com bubbles, when people were expecting to be billionaires but suddenly, they did not earn anything. What was actually happening in 2002 is that people in the dot-com world were trying to create new business models, new business infrastructure and new consumer behavior, simultaneously. Whereas what we have today is vastly increased computing power and improved user access.

We were talking about mobile payment in the last session. Some studies show that by 2020, there will be six billion smart phones in the world. Six billion means one smart phone for every person in the world. This is not true today for India at present, not true for Africa, but if we see the incredible advance of the smart phone, it means the user access is pretty much ubiquitous. Finally, we are seeing exponential adoption speed for new technologies or innovations. Think, how long it took for radio or television, for that matter even for a mobile phone, to be adopted or how long it took for Amazon to get a billion customers, for Facebook to have a billion users, for an app to reach a billion people and it is now



* Managing Director & Global Leader of Financial Services, Deloitte,

down to days or even hours in some cases, the speed of adoption is something which we have never seen before. So, what the financial services are trying to do is that, they are trying to create new business models, and thereby change or improve the customer experience. But they are not trying to introduce to the customers something which has not been done before. Rather, they are trying to introduce new business models with the background of this incredible change in technology that is driving their growth.

I will now be sharing with you a part of the report of the World Economic Forum where I had a role to play. Beginning of 2014, we were asked to look at how disruptive innovations are shaping the way the financial services are structured, provisioned and consumed. This basically boiled down to three questions. Which one of these innovations is actually the most impactful and relevant to financial services? How these innovations will impact the way financial services will be delivered or consumed or structured? What is the impact of all these going to be and what will be the implications of this change on customers, the institutions themselves and on the overall financial services market?

What we did was that we worked with a large number of stakeholders in the financial services, industry leaders, innovators and we held a number of working sessions with participants of the world. I just want to share one observation which I was reminded of in the last session by a participant who was talking about Wells Fargo and I know Mr. John Stumpf, CEO, Wells Fargo reasonably well. I invited Mr. John to speak at a conference we held in 2012, in Istanbul, and I asked him to speak on the subject of mobile banking and the impact that it was going to have on general retail banking. Mr. John, at that time, was of the opinion that mobile banking will not have much of an impact. He thought that people still wanted to go into branches or as he called them stores and that this may not change very much in the next 10,15,20 years. Three years later, I invited Mr. John back to speak on the subject of mobile banking. His views had changed completely. He mentioned that he had closed 500 branches of Wells Fargo in the US- and that he is completely revolutionising what those other two thousand branches would be doing in the future. What was interesting in this project was in the first workshop that was held in Davos, there was a healthy degree of skepticism from the industry participants as to whether disruptive innovations are really going to make an impact. During the 2nd workshop which was one year later in Davos, the mood had completely changed. One of the first things that we tried to do in the programme was to get some way of defining what disruptive innovation really means in financial services. We attempted to sort six key areas within financial services such as payments, insurance, deposits and lending, capital raising, investment management and market provisioning and then we tried to map the innovations to these six segments. We then identified 11 clusters to which we could map the innovations. We then examined how the innovations impacted the core functions of financial services. We came up with some of the clusters like “payment rails cassius world” in the payment space, “crowd funding” in terms of capital-raising, “alternative lending mechanisms” in terms of deposits etc. We went in to each of those clusters and looked at the implications of those scenarios on customers, on incumbent institutions and on the overall financial services ecosystem. Innovation in our industry is happening in a very deliberate and very predictable way and the way in which you can predict that in your organization or in your ecosystem is to look at where are the greatest sources of customer friction and where that meets the largest profit pools. And let me just take one example-payments. Why has there been so much innovation in payments? - because payments as a process, historically, have caused enormous customer friction. It was expensive, it was difficult, but it wasn't very timely and actually, it also created for the banks pretty massive profit pools. 33 percent of the profit of most financial institutions is actually linked to the payment mechanism within those institutions. This means that if there's a threat, it is a large threat to the profitability of most banks around the world. Secondly we found that innovations have the greatest impact when business model platforms based on modular data intensive were employed.

Although, everyone talks about the impact on the banking sector, in the long run, the greatest impact may be felt in the insurance sector. The reasons for this are

From our research, we have synthesized 10 unique insights about innovations in financial services (1/3)

What are the common characteristics of innovation in financial services?

1. Innovation in financial services is **deliberate and predictable**; incumbent players are most likely to be attacked where the greatest sources of **customer friction** meet the **largest profit pools**

Alternative Lending	Automated Wealth Management	New Market Platforms
LendingClub, Funding Circle	Personal Capital, FutureAdvisor	ALGOMI, NOVUS, BISON

2. Innovations are having the **greatest impact** where they employ business models that are **platform based, modular, data intensive, and capital light**

Alternative Lending	Automated Wealth Management	New Market Platforms
Kabbage, PROSPER	Personal Capital, Hedgeable	ClauseMatch, LIQUITY, BISON

3. The most **imminent** effects of disruption will be felt in the banking sector; however, the greatest **impact** of disruption is likely to be felt in the insurance sector

Disaggregation of Insurance Value Chain	Connected Insurance
Google, airbnb, Getaround	nest, UPS, SmartThings

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From our research, we have synthesized 10 unique insights about innovations in financial services (2/3)

What are the common characteristics of innovation in financial services?

4. Incumbent institutions will employ **parallel strategies**; aggressively **competing with new entrants** while also leveraging legacy assets to provide those same new entrants with **infrastructure and access to services**

Alternative Lending	Automated Wealth Management
LendingClub, OnDeck	FutureAdvisor, covestor

5. **Collaboration** between regulators, incumbents and new entrants will be required to understand how new innovations alter the **risk profile of the industry** – positively and negatively

Alternative Lending	Decentralized Systems	Smarter, Faster Machines
LendingClub, Funding Circle	bitcoin, ripple, bitpay	AYASDI, PORTWARE, SNTMNT

6. Disruption will not be a one-time event, rather a **continuous pressure to innovate** that will shape customer behaviors, business models, and the **long-term structure of the financial services industry**

Shifting Customer Preferences	Process Externalization	New Market Platforms
fidor bank, SIMPLE	FUNDAPPS, AYASDI, OpenGamma	ALGOMI, NOVUS, BISON

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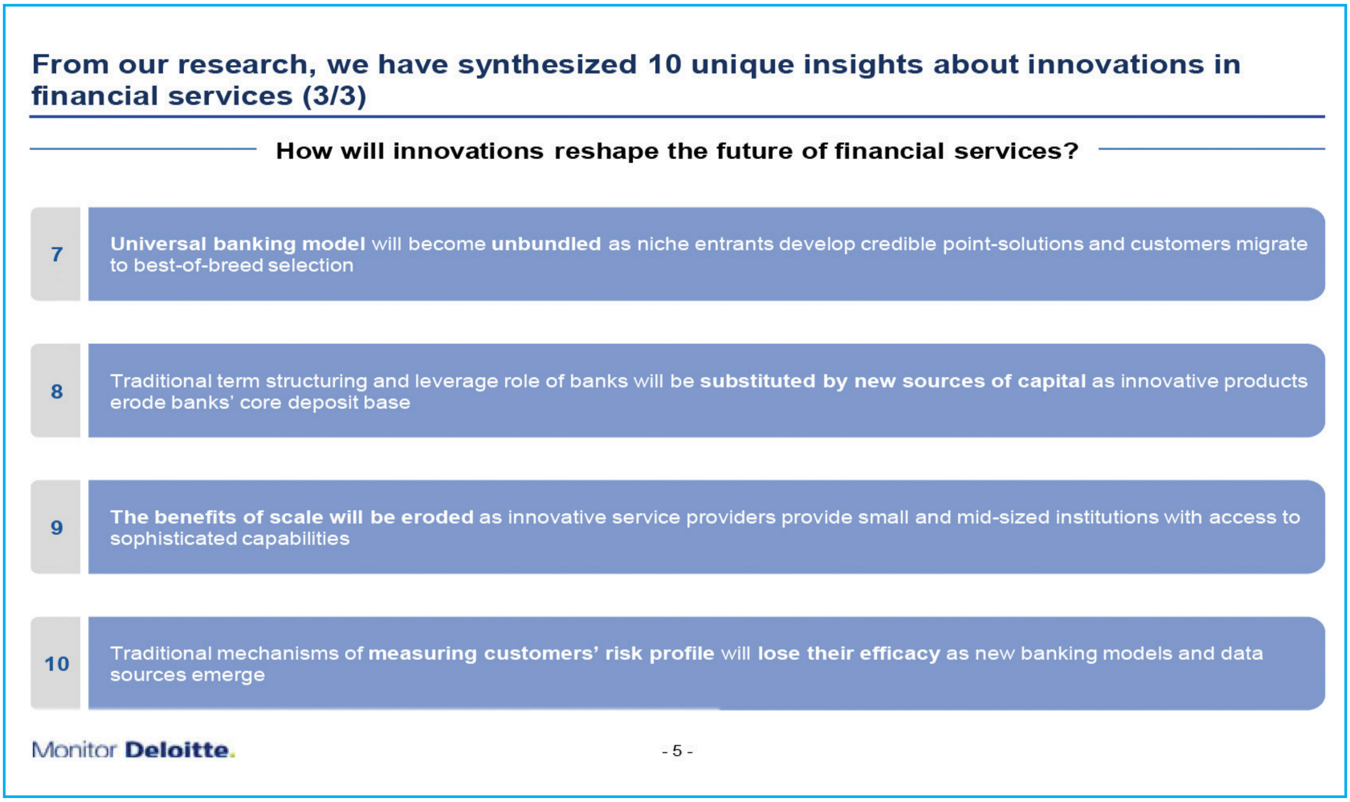

as follows. Firstly there's a graduation of the insurance value chain through new players/new entrants coming into that value chain and taking out some of the value inherent in that and then, this whole concept of connected insurance. I also think one area which we are now beginning to explore in greater detail is how the innovations such as the block chain will affect the way in which people gather and use information for insurance underwriting. The really interesting question is what is the future of the actuarial profession when machines will come up with much more tailored predictions? It is tailored to individuals rather than to groups of middle aged gentlemen. So I think, there is a really interesting impact on insurance. We believe that incumbent institutions will not only employ parallel strategies in terms of aggressively competing with new entrants by leveraging their own assets to give those entrants some infrastructure and access to the market but will also subsume some of those new entrants into themselves. And I think the latter is already happening.

In order to include regulators and governments within the ecosystem to manage the risk profile of the industry, we are now talking, along with the World Economic Forum and ourselves, with regulators into this discussion. One example where it works is WeBank. It is a new bank which has been launched in China. It is actually the banking arm of Tencent. Tencent is a mobile phone operator. Tencent also has a very large online shopping business. We always hear about the Amazons of this world. Tencent-online shopping business has something like 450 to 500 million customers. It also owns WeChat which is the Chinese equivalent of Facebook. What did they do? They took the best from other places, bought them together and created something new. Whether you call it innovation or not, but it is innovative. All three elements are owned by Tencent. People at Tencent said “Well, we're going to apply for a banking licence and go through with the banking licence application and do the business model”. In this case, the regulators actually became part of the project team not necessarily on a day-to-day basis but from a gated basis. The approval process from the regulators was incredibly short and actually, the regulator was involved in the creation of this new bank-WeBank. Why that was so important? - because Tencent were doing something radically new with this bank. Tencent realized that they had extraordinary degree of information about eight hundred and fifty million Chinese customers from their mobile phone records, from their social media records, from their online shopping records they knew so much more about their customers. So what they wanted to do was to use that information to pre-approve customers for current accounts, loans, credit cards etc. When they launched, they had a hundred and forty-seven million customers pre-approved for current accounts, credit cards and revolving credit of other forms and that was all approved by the regulator. My point in the story is by involving the regulator in this innovation; actually we can come up with really new and interesting things. If you manage from a regulatory point of view, the risks will significantly reduce. There will be a continuous pressure to innovate. This pressure will be from customers, regulators and the market in general. This will affect both the business model and the long term structure within the industry. Innovation has to become part of the life blood of any organization. Most of the institutions are saddled with legacy. Legacy comes at a cost. Replacing legacy comes at an even higher cost. In fact I read only yesterday of a new bank that's launched in the UK which has no back office and no front office. It's interesting that they basically outsource everything to other players. You focus on specific products, specific markets or specific segments where you really believe you can build sustainable competitive advantage. How do you protect your customer relationships without providing those universal services, if that's the way you decide to go, what are these products and markets and segments that you want to be or will be in the future and how do you maintain profitability when you're being pushed into lower margin products and services. I've been working in financial services. The common belief in many places is that the fact that our deposit takers insulate us from the worst effects of change because in pretty much every jurisdiction, you have to be a regulated entity to become a deposit taker. Yes, but think about what Alibaba and Alipay are doing in China. Is it not deposit-taking? They were not regulated and they made a ton of money and more importantly, they siphoned deposit out of the banking system. This is an example of a potential danger. The questions for the future are: will you and can you still continue to fund your investments through retail sources of capital or do we have to rely more on wholesale funding and capital markets? How will you evolve your core propositions to avoid potential erosion in the core deposit base of your institutions? How will you protect the margins particularly against those institutions which will be specializing in financial engineering? One of the other great beliefs that have been held as a universal truth as someone once said is that “scale matters”. I'm big and therefore it's really unlikely that I'm gonna be attacked or taken out. Well we are seeing, as I mentioned, the bank that has no back office and no front office; new entrants into the market where scale doesn't matter, sizes not important in certain aspects of their businesses. So you know there are processes now. They're going to be freely available as a service in the cloud, which will give organizations access to sophisticated capabilities. That hitherto had only been possible within the large-scale monolithic systems that sit within financial institutions. Traditional mechanisms of measuring customers risk profile will lose their official efficacy as new models and new data sources emerge. In the last session of the conference, someone also mentioned potential use of social profiling, social media center in the banking system. This is happening today and in fact we're involved in a pilot project in Peru. In this project, two banks have started using a psychometric profiling system to look at the creditworthiness of potential customers. These customers much like many customers in India were people without any credit record/history, were new to credit, new to the market. There was nothing really to go by in terms of credit records. They used psychometric profiling which was designed by a professor at Harvard. It looks at what we know about one’s character and the sort of person one is. What we found in the pilot was, this particular approach was something like forty or fifty percent more likely to predict non-performing loans than traditional credit scoring methods. So I think scoring mechanisms will become less relevant. I think we need to start thinking about how we can use some of this new technology to drive much more individualized ratings and assessments of our customers and their propensity to buy to sell or to order or to repay in the case of a loan. I would like to come to the starting point of my speech. My own view actually is that most financial institutions will not die and wither on the vine. I think most of you understand this and will start to take on the challenge. To take up the challenge, you will have to break some eggs along the way because you will be running up against some very entrenched views and behaviour within your organizations. It is a not just a technology issue. But it is a massive change management issue including the change the way in which your people think, the way in

Universal banking model will become unbundled as niche entrants develop credible point-solutions and customers migrate to best-of-breed selection

Lean and nimble niche new entrants will create **margin pressure** on banks' individual products

Niche entrants will gain customers' trust and condition customers to **shop best-of-breed products**

Non-traditional technology players will create **digital marketplaces** that disaggregate customer relationship and enable comparison shopping

Universal banks will become unbundled

- Price competition will intensify in each product and customer segment
- Banks' universal ownership of customer relationships will be challenged
- Banks' ability to cross-sell products will be reduced
- Cross-subsidized product and margin structure will act as a competitive burden

Key questions for financial institutions

- Will you remain as a universal bank or focus on specific products, markets or segments?
- How will you protect the universality of customer relationships without providing universal banking services?
- What are the products, markets and segments you will participate in the future?
- How will you maintain profitability on distribution of low margin products in areas where you choose not to participate in?

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Traditional term structuring and leverage role of FIs will be substituted by new sources of capital as innovative products erode banks' core deposit base

Customers will become empowered to directly invest capital to **new asset classes** that were previously restrictive

Retail banks' **core deposits will become eroded**, limiting banks' lending capacity ability to match treasury

Platform-based new entrants will open doors for **institutional capital to participate in retail market**, increasing the total supply of capital

New sources of capital will substitute banks' role

- Total amount of capital available to banks will be reduced
- Banks' capital will generate lower return on average
- Competitiveness of traditional term structure and leverage will be reduced
- Banks' flexibility to react to changes in market environment will be limited

Key questions for financial institutions

- Will you continue to fund your investments through retail sources of capital or increase reliance on wholesale funding?
- How will you evolve your value propositions to prevent the erosion of core deposits?
- How will you protect the margins on your products against institutions that specialize in financial engineering?

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The benefits of scale will be eroded as innovative service providers provide small and mid-sized institutions with access to sophisticated capabilities

The new generation of process externalization will provide an **economical access to sophisticated capabilities**, no longer dependent on banks' ability to make heavy infrastructure investments

New market platforms improve the **flow of information** so that more transactions will be conducted based on **fact-based merit**, rather than relationships or reputation

New digital distribution channels will improve financial institutions' **scalability at an exponential rate** by reducing the importance of physical presence to reach customers

The benefits of scale will be eroded

- Changes to the market composition and competitive dynamics will be accelerated
- The benefits of mass market approaches will be reduced
- Niche institutions specialized in products, customer segments and markets will be empowered to emerge

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Traditional mechanisms of measuring customers' risk profile will lose their efficacy as new banking models and data sources emerge

Cashless payments will displace the credit card usage with bank account-funded transactions, **depleting accumulation of payment history**

Unbundling of universal banking model will disperse customers' financial portfolio across multiple best-of-breed providers, limiting a single institution's ability to **fully understand customers' financial health**

New entrants will gather and use **new data sources** to improve the accuracy of risk assessment, leading to **adverse selection** and reducing profitability of institutions employing traditional credit scoring models

Traditional average-based scoring systems will become less relevant

- Centralized credit scoring system will be replaced with decentralized models of individualized risk assessment
- Financial institutions will have a greater impetus to understand customers' lifestyles
- Financial institutions and new entrants will be incented to participate in collaborative data sharing

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- 10 -

which your managers manage and the way in which your organization works in the future. It is a big change and challenge. But I actually believe that most financial institutions are up for that. If the regulators come to work alongside with financial institutions and governments can support, then I think we have the basis for a good way forward. Some of the findings from the next stages I think are going to be quite interesting because we've been asked now to look at some further issues. The first one is what are the regulators going to do and how can we better partner with regulators and financial institutions and entrepreneurs in that ecosystem to make this work in the future? The second thing that we're going to do is looking at digital identity. Is there a way in future that we can have a single repository of digital identity all around the world, eight million people or whatever, it will be by then so that we can really know our customers?

We will come up with some protocols around which we can then have a common set of characteristics of what a digital identity might look like and then we can take it forward.

SEBI Framework for fund raising by start-ups

The Institutional Trading Platform (ITP) is accessible to companies which are intensive in their use of information technology, intellectual property, data analytics, bio-technology, nano-technology to provide products, services or business platforms with substantial value addition and with at least 25 per cent of the pre-issue capital being held by Qualified Institutional Buyers (QIBs), or any other company in which at least 50 per cent of the pre-issue capital is held by QIBs.

Further, no person (individually or collectively with persons acting in concert) in such a company shall hold 25 per cent or more of the post-issue share capital.

Only two categories of investors, i.e. (i) Institutional Investors (QIBs along with family trusts, systematically important NBFCs registered with RBI and intermediaries registered with SEBI, all with net-worth of more than ₹5 billion) and (ii) Non-Institutional Investors (NIIs) other than retail individual investors can access ITP.

The disclosure by the companies may contain only broad objectives of the issue and there shall be no cap on amount raised for ‘General Corporate Purposes’. As the standard valuation parameters such as P/E, EPS etc., may not be relevant in case of many such companies, the basis of such issue price may include other disclosures, except projections, as deemed fit by the issuers. In case of public offer, allotment to institutional investors may be on a discretionary basis whereas to NIIs it shall be on proportionate basis. Allocation between these two categories shall be in the ratio of 75 per cent and 25 per cent respectively. In case of discretionary allotment to institutional investors, no institutional investor shall be allotted more than 10 per cent of the issue size. All shares allotted on discretionary basis shall be locked-in, in line with requirements for lock-in by anchor investors i.e. 30 days at present. The minimum application size in case of such issues and the minimum trading lot is ₹1 million. The number of allottees in case of a public offer must be more than 200. The company is given the option to migrate to main board after 3 years subject to compliance with eligibility requirements of the stock exchanges.

Source : Financial Stability Report, Issue No. 12, Reserve Bank India, December 2015

BOOK REVIEW

Name of the Book : Smart Manager - Retail Banking Decoded

Author: Ms. Poppy Sharma

Publisher: Taxmann

Pages: 180 (Edition 2015)

Price: ₹ 195/-

Reviewed by: Mr. Avinash Chander Mahajan, Chairman, Banking Codes & Standards Board of India.

In a liberal India economy, driven by market forces, the competition among financial intermediaries / businesses is so fierce and tough that only the strong will survive. Strong doesn't mean physically strong. It means emotionally & mentally strong. It means being educated on your business, industry and , customer. It means treating the customer the same way you wished yourself be treated. It means considering the customer as a most important person in your professional life and under no circumstances, to consider him/her business potential may be . It means communicating with your employees and your customers. And it means being prepared and ready each business day to serve the customer in best possible way, no matter what is happening in the economic marketplace. It is well established fact that in business and in this economy, only the strong and who changes fast according to time survive... and win.

To ensure success in the market place, it is necessary to have affirmative answers of following

1. Do you know, how to acquire new customer and retain the existing customers?
2. Do you market your services to your existing customers through communication and effective channel usages by leveraging all channels?
3. Do you understand your customer's changing tastes? Do you change your strategy to meet customers changing needs?
4. Do you continue to train and educate your staff and yourself and communicate your service philosophy to them through structured arrangement in the branch?

5. Are you customer friendly Executive who will keep customer ahead of staff?
6. Whether your staff give their best they can be or just show up every day?
7. Do you behave similarly yourself and keep your organization ahead of yourselves?
8. Do you ensure a punishment for the delinquent employee because of rude, bad behavior or nonperformance?
9. Do you follow a system of face to face appraisal of Employee performance which induces an employee to excel in his/her KRA evaluation?
10. Does the appraisal is a done strictly on merit and performance and not all on personal equation?
11. Do you reward and recognize extraordinary performance of helpful employee who go extra mile only to ensure that customer remains happy and retained?

I am very happy to note that the book, SMART MANAGER, Retail Banking Decoded by Ms. Poppy Sharma, Member Faculty Central Bank of India, exactly deals with all the above thoughts on how to compete and develop retail portfolio at a branch in fiercely competitive market place.

The book written in a class room lecture style, teaches the reader as to how to conduct himself/herself after assuming charge of a bank branch for developing branch business especially retail portfolio of branch. By following the advice detailed in various chapters especially chapter 3, 4 and 5, a Branch Manager will able to build long term relationship with the customers and therefore, prove himself/herself a SMART MANAGER who considers excellent customer service as a Business Philosophy.

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3) Autobiographical note and photograph:
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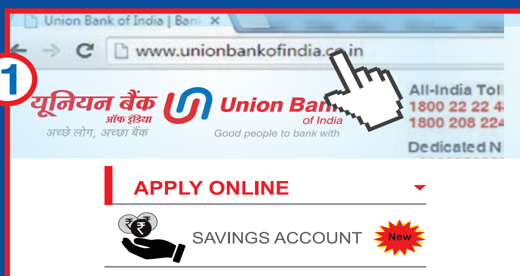

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