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FIBAC 2016

"New Horizons in Indian Banking"

16th -17th August, 2016

Programme

16th August, 2016	
9.30 a.m. - 10.45 a.m.	**Inaugural Session**
	Welcome Address by: Mr. Harshavardhan Neotia, President, FICCI and Chairman, Ambuja Neotia Group **Brief Remarks by:** ❖ **Mr. Ashwani Kumar**, Chairman, IBA and CMD, Dena Bank ❖ **Mr. Arun Tiwari**, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India **Release of Knowledge Paper and Launch of the 'FIBAC 2016 Benchmarking Digital Tools'** **Presentation on the theme of the conference by: Mr. Saurabh Tripathi,** Senior Partner and Director, BCG India **Inaugural Address by: Dr. Raghuram Rajan**, Governor, Reserve Bank of India **Vote of Thanks by: Mr. Rajeev Rishi**, Deputy Chairman, IBA and CMD, Central Bank of India ***Session Moderated by: Dr. A Didar Singh,*** *Secretary General, FICCI*
10.45 a.m. - 11 a.m.	**Tea/ Coffee Break**
11 a.m. - 12.30 p.m.	**Session on 'New Horizons in Indian Banking'**
	Moderation by: Mr. Saurabh Tripathi, Senior Partner and Director, BCG India **Panel of Speakers:** ❖ **Mr. Ashwani Kumar**, Chairman, IBA and CMD, Dena Bank ❖ **Mr. Rajeev Rishi**, Deputy Chairman, IBA and CMD, Central Bank of India ❖ **Ms Arundhati Bhattacharya**, Deputy Chairperson, IBA and Chairman, State Bank of India

	❖ **Mr. Shyam Srinivasan**, Managing Director and CEO, Federal Bank ❖ **Mr. Vishwavir Ahuja**, Managing Director and CEO, RBL Bank ❖ **Mr. Pramit Jhaveri**, CEO - India, Citi ❖ **Ms Roopa Kudva**, Managing Director, Omidyar Network India Advisors
	Q&A
12.30 p.m. - 1.45 p.m.	**Sessionon 'Resolution and turn around management'**
	Turn the financial challenge to an opportunity? Restructuring and turnaround is a very critical skill that is required in the current market environment. With many key accounts having high potential of going bad, banks need to actively think through ways of participating in the success of the turnaround of a corporate. Are there innovations and new practices that can support a better outcome for the corporate, financial institutions and other parties? The banking regulators new norms for Strategic Debt Conversion (SDR) which will give lenders the right to convert their outstanding loans into a majority equity stake if the borrower fails to meet conditions stipulated under the restructuring package as also opens up many new avenues to rethink restructuring in the traditional sense. Banks need to think through new ways to manage the restructuring and turn around management of these companies and work out what value added services to add to their portfolio - financial advisory and business management. **Presentation by: Mr. Rahul Jain**, Partner, BCG India **Panel of Speakers:** ❖ **Mr Dinesh Kumar Khara**, Managing Director, State Bank of India and ex-CEO and MD of SBI Mutual Funds. ❖ **Mr. Arun Tiwari**, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India ❖ **Mr. Rashesh Shah**, Vice President, FICCI and Chairman and CEO, Edelweiss Group ❖ **Ms Zia Mody**, Senior Partner, AZB & Partners ❖ **Mr. M R Umarji**, Consultant, Indian Banks' Association
	Q&A
1.45 p.m. - 2.45 p.m.	**Lunch Break**
2.45 p.m. - 3.15 p.m.	**Special Address on "Banking Horizons: Clouds and Silver Linings" by: Mr. S S Mundra**, Deputy Governor, Reserve Bank of India

3.15 p.m. - 4.30 p.m.	**Session on 'New ways to do credit andmonitoring in the new age world'**
	In times of volatility and fluctuations in the market, financial institutions need to prove their mettle by withstanding the market variations and achieve sustainability in terms of growth and well as have a stable share value. By the nature of their business, banks collect a lot of data on their customers. But they are far behind some of the non-banks in being able to use that information to either improve customer service or predict customer behaviours. Banks need to leverage customer behavioursie. Transaction data, historical trends and marry it with social credit bureau and other proprietary market data through ecosystem partnerships to predict customer behaviours and be able to provide credit. It's a new world where credit can be a push rather than a pull from the customers. Significant portion of new credit will be straight through-super simplified and not requiring any human intervention. As technology innovations and data analytics pick up pace, it will become critical to leverage Bank's large customer behavior and transaction databases to set up early warning signals as well as tailor services, products and offers based on risk profiling of customers. An efficient risk management framework is paramount in order to factor in internal and external risks. **Moderation by: Mr. Ruchin Goyal**, Partner, BCG India **Panel of Speakers:** ❖ **Mr. Rajnish Kumar**, Managing Director (National Banking Group), State Bank of India ❖ **Ms Zarin Daruwala**, CEO - India, Standard Chartered Bank ❖ **Mr. V Srinivasan**, Deputy Managing Director, Axis Bank ❖ **Mr. Satish Pillai**, Managing Director & CEO, CIBIL ❖ **Mr. Ajay Pandey**, MD and Group CEO, GIFT City ❖ **Mr. Abhishek Bhattacharya**, Co-Head -Banks and Financial Institutions, India Ratingsand Research ❖ **Mr. Vikrant Chowdhary**, Head - BFSI and Telecom, SAP Indian Subcontinent
	Q&A
4.30 p.m. - 6 p.m.	**Session on 'New ways of leveraging technology and ecosystems for changing business growth'**
	Leveraging digital technology will be critical to changing the trajectory of traditional business growth and new digitally enabled transaction banking can unlock much more profit pools from this evergreen business. Although the penetration across the different channels has been underwhelming

	considering the strong penetration by other sectors like e-commerce in the country. Banks today are exploring many opportunities to grow their business and introduce new products in to the market. Adoption of IT for banking services offers unprecedented convenience, cost-effectiveness and speed of delivery and in recent years we have seen a significant adoption of these alternate channels across the country. Indian banks are moving to digital and using social, mobility and cloud based business models for transactions, cyber-threats are bound to increase. Partnership offers a new way of working where a partner can come plug in a capability or skill difficult for a bank to meet or become a new sales channel for the Bank. In the tumultuous Indian financial sector market, we have recently seen an unprecedented number of partnerships and many more in the pipeline. Banks are even taking a step forward by integrating with new channel partners to allow straight through processing and use advanced analytics based lending to increase conversion rates while reducing risks. The opportunities are galore and banks need to review and leverage technology as a way for sustainable growth. **Moderation by: Mr. Ashish Garg**, Partner, BCG India **Panel of Speakers:** ❖ **Mr. Ajit Rath**, Executive Director, Andhra Bank ❖ **Mr. Rajiv Sabharwal**, Executive Director, ICICI Bank ❖ **Mr. Sharad Mohan**, Country Head - Retail Banking, Citi India ❖ **Mr. Rajiv Anand**, Executive Director, Axis Bank ❖ **Mr. Nishant Singh**, Founder and CEO, CRMNEXT ❖ **Mr. Arindam Mukherjee**, Operations Director - Enterprise Business, Cisco India and SAARC
	Q&A
6 p.m. onwards	**Networking Reception**

17th August, 2016	
9.45 a.m. - 11 a.m.	**Session on 'Voice of Corporate and SME Banking Customers'**
	The session will be based on extensive corporate and SME survey. FIBAC customers' survey will comprehensively assess the changing needs of Corporate & SME customers. Four tiers of customers across segments and will be assessed including Large (>1000 Cr), Mid (250 to 1000 Cr), Small (50-250 Cr) and Very small (<50 Cr). The survey will cover key corporate banking segments including transaction banking, lending, investment banking, treasury and advisory. The survey will assess and calibrate current performance across the banks on factors such as advocacy / willingness to recommend a bank, importance of various product attributes, satisfaction levels across product/ services as well as strengths and improvement areas for banks. It will be highly beneficial in identifying changing trends in requirements and expectations of the SME and corporate segments and highlight innovations required to better cater to this large and growing segment. **Moderation by: Mr Bharat Poddar**, Partner and Director, The Boston Consulting Group, India. **Panel of Speakers:** ❖ **Ms Usha Ananthasubramanian**, MD and CEO, Punjab National Bank ❖ **Mr. Rakesh Singh**, Chief Executive Officer, Aditya Birla FinanceLtd. ❖ **Mr. Sanjay Bhatia**, Managing Director, Hindustan Tin Works and President, FICCI-CMSME ❖ **Mr. Rajat Verma**, MD and Head - Corporate Banking, Commercial Banking, HSBC India
	Q&A
11 a.m. - 11.15 a.m.	**Tea/ Coffee Break**
11.15 a.m. - 12.30 p.m.	**Session on 'Capitalization challenges and new Basel norms for the new frontiers in risks'**
	Chair: Mr. P K Gupta, Managing Director (Compliance and Risk), State Bank of India **Panel of Speakers:** ❖ **Mr. Melwyn Rego**, MD and CEO, Bank of India

	❖ **Mr. G Gopalakrishna**, Director, CAFRAL ❖ **Mr. Mohan Jayaraman**, MD, Experian Credit Information Company of India Pvt. Ltd. and Country Manager, Experian India ❖ **Mr. Abhishek Bhattacharya**, Co - Head, Banks and Financial Institutions, India Ratings and Research
	Q&A
12. 30 p.m. - 2 p.m.	**Session on 'Transaction Banking: New Frontiers with Digital and Technology'**
	New digitally enabled transaction banking can unlock much more profit pool from this evergreen business. Current digital offerings, if any, by Indian corporate banks, are stand-alone products with limited integration. It is not uncommon for a customer of a corporate bank to have four or five different digital products from the same bank-each with its own credentials, security, sign-on and user interface. Most banks are organizationally structured to sell products. This arrangement works well in a growth environment where there is enough market demand to open new avenues and meet targets. However, this model quickly breaks down when the game shifts towards garnering a share of the wallet to grow profitably and efficiently. Garnering a share of the wallet requires cross-selling multiple products to the same customer. But banks that have created integrated solutions to address the end-to-end value chain and have digitally linked the whole experience have gained disproportionate market share in that value chain. Few banks have looked at these problems end-to-end from the value chain perspective. Banks / non-banks that have created end-to-end digitally linked platforms for transacting across the value chain have generated significant efficiency in the system, created stickiness for their own products, garnered higher share of the wallet and established unassailable market position in niche sectors. **Moderation by: Mr. Prateek Roongta**, Partner, The Boston Consulting Group **Panel of Speakers:** ❖ **Mr. M K Jain**, MD and CEO, Indian Bank ❖ **Ms Debopama Sen**, Head, Treasury and Trade Solutions, Citi India ❖ **Mr. Rajeev Ahuja**, Head - Strategy, RBL Bank ❖ **Mr. Asit Oberoi**, Group President and Global Head, Transaction Banking Group, Yes Bank ❖ **Mr. Abhay Gupte**, CEO,Manipal Technologies Ltd.

	❖ **Mr. Kiran Shetty**, CEO, SWIFT India **Q&A**
2 p.m. - 2.45 p.m.	**Lunch Break**
2.45 p.m. - 4 p.m.	**Session on 'Robotics and Artificial Intelligence: Ultra productive operations'**
	Robotics and AI can help re-imagine banks business processes with many inherent benefits - lower costs, optimize quality, enhance productivity and be at the fore-front of technology evolution. A digital workforce and tools can create a seamless back office. The automation, artificial intelligence and machine learning capabilities can be used for creating a digital workforce that can be used to setup a seamless backup office but can be extended to do wealth management, start the next wave of customer product and service. A simplistic example is the digital vault that has already been introduced in India that leverages the robotics technology to provide 24x7 services to customers using lockers. Artificial intelligence, machine learning and deep learning will help drive the next revolution in banking by driving significant savings, faster time to market, enhanced business insights, better regulatory compliance and transformation of core business processes. **Moderation by: Mr. Yashraj Erande**, Partner, BCG India **Panel of Speakers:** ❖ **Dr. A S Ramasastri**, Director, IDRBT ❖ **Mr. Mrutyunjay Mahapatra**, DMD and CIO, State Bank of India ❖ **Mr. Sandeep Sharma**, Managing Director, South Asia, NICE ❖ **Mr. Subir Mehra**, Global Head of Operations - Global Service Centres, HSBC ❖ **Mr. Nitin Chugh**, Country Head - Digital Banking, HDFC Bank ❖ **Mr. Pankaj Sharma**, Executive Vice President, Retail Operations, Axis Bank
	Q&A
4 p.m. - 5.15 p.m.	**Session on 'New performance paradigms: Getting used to highly transparent and measurable world'**
	Employee performance has been an elusive topic for many decades especially in most Indian banks. New technology is causing a paradigm shift in performance management providing ways to create a highly transparent and measureable world. The disruption offered by technology is a double edged sword on the talent market. Incumbents need to adopt key elements of HR

	practices of the talent magnet firms like Google, Apple and Amazon to attract and retain new talent. Performance measurement can become highly transparent leading to creation of new performance oriented culture. Existing staff can be enabled with technology tools on their mobile phones that can help them execute tasks and achieve productivity hitherto considered very difficult. **Moderation by: Mr. Amit Kumar**, Partner, BCG India **Panel of Speakers:** ❖ **Mr. Sushil Muhnot**, CMD, Bank of Maharashtra ❖ **Mr. Ashwini Mehra**, DMD & CDO, State Bank of India ❖ **Mr. Amitabh Singh**, General Manager - HR, ICICI Bank ❖ **Ms. Rajkamal Vempati**, Head - HR, Axis Bank ❖ **Ms. Vibha Shukla**, Director & Head - HR, SAP India Pvt. Ltd.
	Q&A
5.15 p.m. - 6 p.m.	**Valedictory Session**
	Valedictory Address by: Mr. R Gandhi, Deputy Governor, Reserve Bank of India

*(L-R) **Dr. A Didar Singh**, Secretary General, FICCI, **Mr. Arun Tiwari**, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India, **Dr. Raghuram Rajan**, Governor, Reserve Bank of India, **Mr. Harshavardhan Neotia**, President, FICCI and Chairman, Ambuja Neotia Group, **Mr. Ashwani Kumar**, Chairman, IBA and CMD, Dena Bank, **Mr. Rajeev Rishi**, Deputy Chairman, IBA and CMD, Central Bank of India, **Mr. Saurabh Tripathi**, Senior Partner and Director, BCG India.*

Inaugural Session

Welcome Address: Mr Harshavardhan Neotia, President, FICCI and Chairman, Ambuja Neotia Group

Mr Neotia thanked Dr Raghuram Rajan for his immense contribution towards the growth of the Indian economy and the banking sector. He lauded his exemplary work as the RBI Governor to steer the Indian economy through one of its toughest times, making India emerge as one of the fastest economies in the world. He provided the much needed stability to the economy by taking some well-thought and adept measures.

Mr Neotia observed that "the Indian banking industry is evolving at a phenomenal speed." This transformation, he observed, is driven by a number of factors such as technological development; introduction of new digital payment services, taking us towards becoming a "less-cash society"; changing consumer perceptions; and progress on the financial

inclusion agenda of the Government.

He added that technological advancement in the sector has been beneficial for both the banking community and the consumers. It has led to a complete change in the way banking operations are being conducted. Banks have been able to enhance their geographical reach significantly, and their confidence in carrying out transactions has increased.

This is an exciting phase, but there are various challenges that the banking sector has to overcome

- Capitalisation challenges with respect to adherence to the Basel norms;
- Dealing with stressed assets;
- Adapting to the rapid technological and/or digital changes with their concomitant challenges of threats to cyber security;
- Redundancy of existing systems and practices;
- Disruption of the banking industry due to rapid inroads by fintech companies into areas traditionally serviced by banks.

The Government and RBI are taking measures to address these challenges. Individual banks are also realigning their strategies to embrace the transformations in the industry. The FIBAC programme, jointly developed by FICCI and IBA, has been instrumental in bringing together key stakeholders for a healthy discussion on the challenges faced by this sector.

He concluded with a request from the industry to bring down the interest rates. While the policy rates have been brought down, "the transmission has been less than complete." He hoped the downward revision in interest rates would happen faster. "Yes, Sir, yeh dil maange more!" he implored.

Brief Remarks by Mr Ashwani Kumar, Chairman, IBA and CMD, Dena Bank

Mr Ashwani Kumar began by saying that during the tenure of Dr Rajan, the banks felt very comfortable because they were taken into confidence when decisions had to be made. He added that it was a privilege to be with this audience. The acceptance of FIBAC over the last 12 years could be gauged from the overwhelming response it receives.

He pointed out that competition in the financial sector is increasing. Banks now have to compete with each other and also with other players in the market, such as microfinance institutions, NBFCs, housing finance companies, fintech companies, etc. at all levels, not only on various types of products. From a banker's point of view, the loyalty of a customer to the bank should be top priority; in reality, it is a thing of the past because the customers "move very fast and the loyalty factor is lost." In his opinion, the differentiating factor for all players could be the way they deliver services, and the way they make these services cost effective through adoption of technology. These two factors would be the primary reason for customers to remain with a bank.

According to the latest Performance Against Customer Expectation (PACE) Index report that was released in May 2016, bank customers first turn to the primary financial institution for their financial needs. Those institutions must be prepared to serve their needs immediately. They must also understand the increasing consumer demand for user-friendly banking products and services and develop them to retain their customers. Face-to-face banking remains a very important area even as branches become irrelevant; institutions must strike a balance between digital and face-to-face banking.

The global average of the PACE index is 79 out of 100. India's score is 74, indicating areas where the gaps are wider than the expectations of the customers. Up to 28% of primary institutions face possible loss of customers because they get better service at other institutions. Indian banks fare better in safety, security and channel presence but fall below the expectations of the customers in meeting their aspirations and providing customised services.

As banks move into the digital era, security aspects are an area of prime concern. Measures are being taken by banks to secure their transactions and improve the confidence of their customers. RBI has also recently come up with draft guidelines on cyber security.

He wished the conference a great success.

Brief Remarks by Mr Arun Tiwari, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India.

Mr Tiwari described FIBAC as a premier annual banking conference which is "one of the most sought after events in the calendar of the finance fraternity, drawing participants from all walks of life in India and abroad."

He described the world as being in a state of flux, whether it is the economy, politics or society. "We are living in the most interesting and exciting times," he said, explaining that the centre of economic gravity is "gradually but certainly moving towards Asia." This has implications for the conventional approach to trade, investment and finance. The changing demography is a major force which is shaping demand. "India is where the real action is," he stated, highlighting the abundant promise that it holds with the working age population reaching its golden phase.

But that could also be a double-edged sword, he cautioned. "It can lead to prosperity or perpetual chaos, depending on how we manage the transition." Banks must understand the aspirations of the impatient youth. And he was pleased to declare that they are moving in the right direction.

Another notable force that Mr Tiwari identified is the deepening of information and communication technology in developing economies. The world is becoming a "cellular republic," where Twitter and Facebook netizens influence the political narratives of the day. These developments have a bearing on the way the banking industry does business. Banking is being redefined by a combination of disruptive business models, regulatory interventions and digital innovation.

There are the challenges of costs. Asset quality and capitalisation imperatives continue to drag the business of most banks. The aggregate growth of banks is at the lowest in the decade.

But he was optimistic that these challenges can also usher in a paradigm shift in Indian banking. Banks are now working to raise their efficiency ratios. They are re-evaluating their human resource management, product and process infrastructure, risk management practices, CRM, analytics and technology efficiency. The twin forces of competition and consolidation are at play simultaneously. RBI is now open to "issuing licenses on tap." More competition will enhance efficiency and lower the cost of intermediation. With the opening of 228 million new accounts through the Pradhan Mantri Jan Dhan Yojana (PMJDY), Indian banking has become more democratic. If used effectively, the impact will truly be transformative.

'Digital' is the buzz word today. Technology is being leveraged to create a performance-oriented work culture. Blockchain, robotic process automation, artificial intelligence, crowdfunding, crowdsourcing etc. can help banks reduce their transaction costs, respond to cyber security threats, optimise capacity utilisation, provide frictionless customer experience and ensure meaningful financial inclusion.

He concluded by observing that Indian banking is on a constant churn. This churn should lead to a healthier, stronger and diverse financial ecosystem in India.

Launch of the Online Benchmarking Survey and Release of the FICCI-IBA Knowledge Paper by Dr Raghuram Rajan

Presentation on the **Theme of the Conference by Mr Saurabh Tripathi**, Senior partner and Director, BCG India

Thanking the Governor for launching the report and digital benchmarking platform, Mr Tripathi remarked that Dr Rajan leaves a "very phenomenal legacy in the industry." He also mentioned that it is a great honour for BCG to be the Knowledge Partner for this event over the last seven years. RBI, he said, is such a great institution because it has institutional memory. Hence he offered four suggestions, confident that "whatever gets started is finished at some point of time."

His first suggestion was about digital. He found something unique about the way the Indian banking sector has leapfrogged into digital innovation. There are very few advanced economies which can claim to have this kind of banking infrastructure. The fintech industry has seen over $ 2 billion of investment. There is now almost a competition between the regulators of different jurisdictions in different parts of the world to create the most attractive environment for financial innovation. "We are at kissing distance in creating an industry which will stand out and attract a lot of investment into India," he predicted, pointing out that some foreign banks take India as the place where they experiment and launch their digital innovations to perfect them. Hence, he felt, for India to become a global leader in this space, policy should be articulated around the regulatory sandbox where banks and fintech companies can experiment together in a controlled, welcoming and easy environment.

His second suggestion was about credit. Huge energy is consumed by the current crisis of bad debt. Although he expressed confidence that we would cross this challenge in time, he was firm in his view that a way has to be found to enhance and increase the capability of the banking system so that this issue does not get repeated. He made a few observations about India: it is still a poor country and wants to become rich at a very fast pace; it has independent institutions; and it has diverse stakeholders with different interest groups. There is no doubt that the risks are going to increase. The industries to which banks lend are themselves facing technological disruption; hence it will be even more difficult for banks to take a long term view on lending. The banking industry must do something about this. There are examples in other parts of the world where banks come together and share data about commercial credit.

The National Payment Corporation of India is owned by the banking system and has done wonders by creating an underlying infrastructure that everybody can use. Indian banks should come together and create a shared utility where data on commercial credit can be shared. Commercial credit can be done when data which is surrogate in nature on payments, bills, employees, management, and a variety of other operating matrices is shared confidentially between banks. Banks can then do credit in a manner that is different from what they did in the past.

The third suggestion was about pricing. This, he was at pains to point out, is one area where enough science and technology has not gone into our banking industry. As a consequence, the industry does not differentiate between high risk and low risk as far as pricing is concerned. Customers are actually made to believe that paying fees to the bank is a bad thing. That leads to overdependence upon the net interest income which in turn makes the banking industry's performance volatile with respect to interest rate changes. Applying more science and technology to how pricing is done can discriminate on the basis of risk and ensure sufficient fee income for the banks that is paid by customers for the value that they derive.

Finally, his fourth suggestion was about the banking structure and how it has been impacted by the NPA crisis. Mr Tripathi felt that promoters and entrepreneurs are now under pressure because they see differentiation only between good and bad projects, but not between good and bad promoters. These sentiments could create a vicious cycle, he cautioned, because "economic cycles are dependent upon sentiments and facts." There is opportunity for people to invest; but they are not investing since they have lost the appetite for taking risk because they feel it is not safe anymore. As banks begin to cherry pick their investments, a number of banks in the middle category may get severely compromised. Whether the resolution of this problem should be left just to the banks or intervention at a higher level is needed merits serious discussion.

Mr Tripathi was strongly of the view that India needs public sector banks. They provide long term capital and bring balance into the system. He ended by thanking Dr Rajan for his relentless efforts over the last three years.

Inaugural Address by Dr Raghuram Rajan, Governor, Reserve Bank of India

Dr Rajan began by thanking the organisers for inviting him to give the Inaugural Address at the FICCI-IBA Annual Global Banking Conference.

One of the most important issues on the minds of bankers, said Dr Rajan, is the Asset Quality Review that was initiated in early 2015-16. It has improved the recognition of NPAs, and provisioning in banks has increased. Many banks, he disclosed, had internalised the spirit of the review and were able to recognise incipient stress early. The focus should now move towards improving the operational efficiency of the stressed assets and create the right capital structure, he suggested.

This would mean action on two fronts: firstly, bringing in new project management teams wherever necessary, either as owners or managers. This entails a creative search for these new management teams. It also calls for structuring an attractive incentive package for management teams who are not owners.

The second requirement is to tailor the capital structure to something reasonable. "Let bygones be bygones," he said. It is necessary to create a capital structure that gives incentives and has the flexibility needed for investment. If the loan is already an NPA, there is no limit to the amount of restructuring that can be done. If it is a standard loan for a project that is struggling, there are a variety of schemes by which a "more sensible capital structure can be crafted for the project."

The real problem, he said, is an unrealistic application of these schemes to particular projects. Often, this is done not because the project benefits from the scheme, but to prevent the project from turning into an NPA. What would be beneficial is a judicious application of the right scheme to the right project. He disclosed that the RBI would continue monitoring the process to see that the schemes are used as warranted. RBI would be happy to receive suggestions and make adjustments to the schemes if required.

Looking beyond stressed assets to the growth of the sector, Dr Rajan observed that these are "interesting, profitable as well as challenging times for the financial sector." Interesting, because the level of competition in the financial system will increase manifold for customers as well as for talent, transforming even the sleepiest areas in financial services. Profitable, because new technologies will open up new business opportunities and bring in new, underserved customers. Challenging, because "competition and novelty constitute a particularly volatile mix in terms of risk."

The next year, Dr Rajan felt, will see a lot of new niche banks begin business. "The next bank may not be a bank," he predicted. It may well be a fintech company. "Fintech is knocking on the door and giving us various new ways of accessing and serving customers." Hence, he cautioned, many new institutions that bankers may not even be aware of today, will soon be a source of competition. But the good news is that many new customers who don't have access to the formal financial system will be drawn into it. Service providers need not be alarmed by the onslaught of competition, because they will have significantly more customers to service. Those increases in volumes will be an enormous source of new profits, he said. Moreover, risks taken will tend to be more sensible because of information technology and risk management techniques.

The single most important advantage that banks in industrial countries have is their ability to manage and warehouse risks. Another advantage is their ability to access liquidity from the central bank. Banks must build on these advantages. Today, India is on the cusp of immense infrastructure projects. Banks will be careful to invest in these projects because of the risk aversion created from past losses. But hopefully, this time the risk can be lowered.

Banks must develop a thorough understanding of the respective industry sector so that more in-house expertise can be brought into project evaluation, including understanding the demand projections for the project's output, the likely competition and the reliability of the promoter. If real risks cannot be mitigated, they have to be shared in a "clever way." Contracts should be drawn up carefully so that the project does not get held up indefinitely if the expected does not happen.

Projects must be drawn up with an appropriately flexible capital structure. They have, until now, had too much debt that was inflexible, not long term enough, and not related to the residual risks of the project; the equity was usually not genuine equity, it was brought in by the promoter, making it essentially another form of debt. So projects need to be designed with significantly more equity and greater flexibility in the debt structure. And in order to create the right incentive structures for promoters to ensure that debts are repayed and projects executed on time, the corporate debt markets need to be involved. Such measures may also make it easier to securitize and sell the project loan in the market. The new Bankruptcy Code should also make arm's length debt more feasible.

A robust system of project monitoring and appraisal is imperative as the project takes off. This should include careful real-time monitoring of costs, so that suspicious transactions are flagged and monitored carefully. And there should be a strong incentive structure for bankers, for projects that succeed. There has to be a reward system for taking the right decisions. The old method of relying on the committee system for decision making may not be sufficient. Any one individual has to take the responsibility for recommending the loan. This does not mean that anybody should be held responsible for one project going wrong; the performance of that individual can be evaluated based on the set of decisions made. And since these are commercial decisions, the question of criminal oversight does not arise. Mistakes will only affect promotions and bonuses.

Dr Rajan felt that the banks' first task would be to use all the new technologies, marrying information technology to financial engineering, to do their existing business better. This will help bankers improve on project evaluation and lending. He suggested that those who build their IT network and enhance their ability to access and serve the people will be rewarded with cheap CASA deposits which can then be used to give loans. Today, everybody seems to be heading towards small retail loans. Dr Rajan questioned this approach. "Are we taking on lower quality risks as everybody tries to target the retail customer?" But, with due diligence, there could be profitable opportunities. Credit evaluation, he observed, is increasingly being done by mining the banks' own data, and also that from social media posts. RBI, he disclosed, feels that it should allow some of these innovations and not be too hasty to regulate. Regulation may come in eventually, not to kill the process, but to aid it.

Since data is now a source of competition how can it be shared in order to make better decisions? "People want to restrict access to their piece of the data while having access to everybody else's data." This is something the industry will have to ponder over. He cautioned that while there is great enthusiasm about fintech and the new forms of lending, many of them have yet to be tested by a serious downturn. It is unclear how responsibilities for recovery will devolve between the intermediary and the investor.

Going forward, banks will not remain sole players. The fintech companies will come, and already some alliances are forming between banks and fintech companies. The bottom line is that with increasing competition and ways of delivering financial services, banks will have to "figure out how to use their traditional, although eroding, advantages such as convenience, information and trust."

RBI would like to encourage the most efficient processes so that the economy and the citizens are benefitted. Ideally, this means being neutral towards institutions, ownership and technology. However, the system is skewed in favour of some institutions and kinds of ownership; hence competition may not always produce the best outcomes. Banks are privileged as well as constrained by what Dr Rajan called the 'grand bargain': low cost insured deposits, liquidity support and close regulation. In return, there are costs imposed on the banks, such as reserves with the central bank at zero interest rates, government bonds and priority sector lending obligations. Public sector banks are further subject to government mandates such as opening of PMJDY accounts, and mandates regarding hiring of staff.

As competition increases, skewing a little this way or that can alter who will win the race. Over the medium term, the authorities should reduce these differences in regulatory treatment so that "the full weight of competition and technological innovations can actually play out." He suggested that some of these differences can be mitigated by paying an appropriate remunerative price instead of imposing the respective mandates. This will encourage banks to compete and the most efficient bank will get the business. Some mandates, such as MSME loans, will become less costly with the new techniques. This should make the priority sector lending more beneficial than it has been in the past.

The regulator is also trying to make the mandates "more understanding of technologies." The meaning of 'branch' can be considered as an example. A quarter of a bank's branches are required to be opened in underserved areas. Is it possible to service the needs of a village population in a more efficient way than setting up a full-service brick and motor branch, thereby covering more villages? Can the definition of 'branch' be redefined? This is being reviewed by an internal RBI committee.

The most pressing challenge for public sector banks is cleaning up the balance sheet; but a parallel task is to improve their governance and management. New talent needs to be recruited, with expertise in project evaluation, risk management and IT, including cyber security. One of the most important developments is the emergence of the Bank Board Bureau (BBB), which consists of eminent personalities, who have taken over the appointment process in public sector banks. The Government still plays a role, but as the BBB gains experience, it will make more sense to let it make those decisions. And with time, it will make sense for decisions to devolve from the BBB to the bank boards, as the former transforms into the Bank Investment Company (BIC) which will be the custodian of the Government's stake in public sector banks.

Public sector banks must improve their practices. "Too many loans are done without adequate due diligence and follow up." The public must be convinced that public sector banks treat large and small promoters in the same way. Banks must convince their stakeholders that they are doing a fair job. Another problem with public sector banks is that they "overpay at the bottom and underpay at the top." This makes it hard to attract top talent. They need experts in specific areas. At the same time, the fact that they overpay at the bottom can be used as an opportunity. They can get qualified people in and offer them prospects for advancement by doing value-enhanced work. What seems like a constraint can actually be turned into strength. Another restriction is the court judgement that prohibits hiring from specific campuses. Public sector banks are required to hire through exams. They can petition the courts to take a more liberal view; but another alternative is to make entrance exams less onerous to take, and announce the results quickly so that people from quality institutions are offered a job before campus placements start. Further, banks must be more liberal in hiring local talent where it is available.

As banks adopt differentiated strategies, they must move away from the common industry-wide compensation structures and promotion schemes to a bank-based model. Employee stock ownership plans will give employees a stake in the future of the bank. Public sector banks have very strong bonds with their customers. This bond should be strengthened to encourage deposits that can come to the banks' aid in time of difficulty. That will be the source of their strength. Bank boards should also reflect on the banks' structure: whether they wish to become small finance banks, or emerge and become part of an all-India network to obtain scale and geographical diversification. This issue will become important as banks clean up their balance sheets.

Dr Rajan was clear that we do need public sector banks. However, they shouldn't be unduly favoured or hampered as competition increases. He felt that the authorities must reflect on their role with regard to the public sector banks. The jurisdictions of the various authorities should be streamlined and overlaps between them reduced. Most of the governance will have to eventually move to the bank's board. The Government will have to exercise control through its board representative who will be chosen by the BBB or the BIC. Wherever possible, public sector banks and their boards should be bound by the same rules as private sector banks and their boards. The Department of Financial Services could then move towards a coordinating and developmental role, overseeing and monitoring government programmes and revitalizing institutions.

RBI would want to withdraw their representative from bank boards and move away from governing banks. They would also want to empower the boards by offering broad guidelines. But this will require legislative change. The formal views of the RBI will evolve over time.

Although he focused on the challenges of the public sector banks, Dr Rajan touched on cyber security, describing it as "an area of emerging challenge for all." He said it would be complacent for anyone to believe that they are well prepared to meet all cyber threats. Quoting an IT expert, he declared, "we have all been hacked, the only question is whether you know it or you don't." The statement, he said, may be alarmist, but it is an antidote to complacency. RBI is working on upgrading the capabilities of its inspectors to carry out banking system audits and detect vulnerabilities in them.

He ended by observing that "we will be living in very interesting times." Whether it is a blessing or a curse is entirely up to us.

At the end of his presentation, Dr Rajan agreed to answer a few questions from the audience. Responding to a question about consolidation versus niche banking, he was of the opinion that there is room for both. Having larger banks, with a component of the loan initially made from corporate debt markets will entail some consolidation. This will allow for better project financing. But niche banks are still very important because they tend to understand small entrepreneurs better.

Discussing the issue about too much debt, he felt that it is important because there are examples of other countries going through tremendous periods of strain on account of too little equity and too much debt build up. He agreed that the amount of equity that is needed can be reduced by mitigating the risks of the project. However, one of the virtues that we have that other emerging markets don't is a very strong equity market. This can be used to raise capital; and this equity can actually pay down some of the debt. It requires a little bit of sacrifice, but it is important for a stable system.

Regarding the MSMEs being subjected to very high rates of interest, Dr Rajan's view was that all over the world, MSMEs pay significantly higher rates of interest than large corporations simply because they are new firms and have no track record. The new Bankruptcy Code should help in resolving entities that fail, so that the cost of financing businesses that are viable may be reduced. The AQR should help in recognising the problem and provisioning for it so that appropriate decisions can be made.

Another issue that Dr Rajan considered was about gender disaggregated data and making bank officials more sensitive to the unmet financial needs of women. He agreed that the RBI should see how this data can be collected and disseminated more widely. And he had no doubt that every part of the financial system calls for equality amongst genders and the Reserve Bank needs to work on it.

Vote of Thanks: Mr Rajeev Rishi, Deputy Chairman of IBA and CMD, Central Bank of India

Mr Rishi referred to the reports emanating from the FICCI-IBA conferences that have been held for almost a decade. They have always been very well received and subjected to intense scrutiny. Expressing sincere gratitude to Governor Dr Rajan, he observed that the gathering was privileged to hear his address, especially because it came with the recognition that they would not be lucky enough to keep hearing it in person henceforth. He also thanked the Knowledge Partner, BCG, and the other organisers for developing the framework of this conference.

*(L-R) **Mr. Saurabh Tripathi**, Senior Partner and Director, BCG India, **Mr. Vishwavir Ahuja**, Managing Director and CEO, RBL Bank, **Mr. Shyam Srinivasan**, Managing Director and CEO, Federal Bank, **Ms Arundhati Bhattacharya**, Deputy Chairperson, IBA and Chairman, State Bank of India, **Mr. Ashwani Kumar**, Chairman, IBA and CMD, Dena Bank**, Mr. Rajeev Rishi**, Deputy Chairman, IBA and CMD, Central Bank of India, **Mr. Pramit Jhaveri**, CEO – India, Citi, **Ms Roopa Kudva**, Managing Director, Omidyar Network India Advisors.*

Session on 'New Horizons in Indian Banking'

Session moderated by **Mr Saurabh Tripathi**, Senior Partner and Director, The Boston Consulting Group, India.

Panellists

- **Mr Ashwani Kumar**, Chairman, IBA and CMD, Dena Bank.
- **Mr Rajeev Rishi**, Deputy Chairman, IBA and CMD, Central Bank of India.
- **Ms Arundhati Bhattacharya**, Deputy Chairperson, IBA and Chairman, State Bank of India.
- **Mr Shyam Srinivasan**, Managing Director and CEO, Federal Bank.
- **Mr Vishwavir Ahuja**, Managing Director and CEO, RBL Bank
- **Mr Pramit Jhaveri**, CEO – India, Citi.
- **Ms Roopa Kudva**, Managing Director, Omidyar Network India Advisors.

Overview by Mr Saurabh Tripathi

Over the next 10 years, India will be standing out as one of the fastest growing revenue pools in

Indian banking in the whole world. At that pace, it will be the third largest banking revenue pool in the world by 2026.

We don't give ourselves a pat on the back for what India has become in terms of its underlying banking infrastructure. Very few countries in the world have 100% coverage with biometric identity. GST has just been passed. In a few years, we will have a huge number of invoices between the value chains of different industries digitised. All that digital data will be accessible to banks to do credit lending.

Some interesting facts emerge out of the research on digital. Last year, digital transactions grew at 40%. This year, they grew at 67%. Next year, we will probably find that the largest number of customer-initiated transactions in Indian banking will be digital. That is one layer of the digital transformation in Indian industry.

A very silent revolution is taking place in self service in Indian banking. Self service machines grew by 80% last year. The ratio between ATMs to SSMs was 90:10 in 2014; it was 80:20 in 2016. It is changing dramatically and this is the second layer of digital banking in India, where huge investment is being made, particularly by the public sector.

And now, the third layer of digital transformation of Indian banking is reaching maturity. Large public sector banks have a huge number of business correspondence (BC) outlets or franchisees, much more than the number of branches. A large number of customer-initiated transactions happen on these BC outlets. This is one area where the public sector has invested. It does not bring in returns quickly, but it has reached the size and maturity where the whole channel can be financially viable. It is not merely a physical channel; it has a human touch. It is enabled by indigenously developed technologies to meet the requirements of the Indian people.

Over the last one year, old fashioned, brick and mortar branches of private sector banks have grown by as much as 19% in metro and urban areas. The transformation of the Indian banking sector is complex and multilayered. There are different customer segments that need different services. The environment is rife for differentiation. Branches in India are alive and active. At least in the next five years the country will witness a bionic situation.

A fairly unrecognised fact is that roughly 30% of employment in the Indian banking industry is either part time or on variable fee access. The fastest growth rate is in outbound sales. This is a kind of 'land grab' in the Indian banking market, where players who have business models can grow aggressively and gain a share.

In a global survey, customers were asked whether they preferred digital banking, face-to-face banking or a hybrid of both. In a country like China, which is 10 years ahead of us in electronic transformation, only 7% of people preferred digital banking. A large number of customers wanted face-to-face or hybrid banking. "This is the hybrid future. The future of banking is bionic and we need to embrace it." The issue is not merely whether banking should be conducted digitally or through the branches; it features multichannel integration of all outlets to create the right proposition for the hybrid.

Talking about bad debts, Mr Tripathi felt that they were part of a vicious cycle, beginning with the promoter community not having the confidence to invest, resulting in no new projects. It becomes difficult to resolve the situation with so many banks involved and so many rules. He cautioned that if this issue is not taken head on, "it can really have serious implication on the economic development of the country." How can the situation be addressed? There are a number of options: (a) Should there be a 'bad bank'? This idea has been mooted and discarded, but it needs a re-look. If all the bad debts are consolidated at one place, a single person can resolve the problem. (b) Is the capitalisation that has been offered to the public sector banks by the government enough? (c) Should the interest rates go down and the bad debts wiped away through treasury profits? (d) Is a surgical approach required, wherein the Government reduces its stake in public sector banks and allows the markets to come in; or allow the banks to transfer the NPAs between each other so that one bank then becomes dominant and can take quick decisions? He was of the view that while something like this is really necessary, it is not being fully appreciated. This may result in some medium sized nationalised banks facing a difficult situation and not being able to focus on development and investment.

India has not invested as much as some other countries in its public sector banks. They need a set of capabilities like paperless processes, digital sales, bionic distribution and non-bank activities. It will not be easy. They will have to rely on partnerships. "Corporate banking will go away from balance sheets to more industry-specific transaction banking solutions." The ones who develop these capabilities are the ones who will win.

Regarding differentiated strategies, Mr Tripathi felt that differentiation could be based on various factors: region, customer category, whether the bank is purely digital, or the kind of bank business — savings and wholesale, savings and mortgage, purely wholesale, or custody banks. Some of these banks do not yet exist in India but are there in other countries.

Mr Tripathi ended by pointing out that India is one of the lowest in the world when it comes to customer-paid fees as a ratio of the NII. "Indian customers have forgotten how to pay fees to the banks and that's not good for the banking industry." He called upon the leaders of the banking industry to discuss this. He also observed that in many other countries, banks have a jointly held entity which allows information to be shared for commercial credit. India also needs an entity like this so that when things get better, banks will have the capability to improve their commercial credit business.

Panellists' Views

Ms Arundhati Bhattacharya

Ms Bhattacharya referred to the chakravyuh of the Mahabharata that Mr Tripathi had alluded to during his talk. "The chakravyuh actually has a way out, it's only that Abhimanyu doesn't know it but Arjun does." The banking industry must now be Arjun and not Abhimanyu. What she meant is that the solution to the problems of the banking industry will not come from outside. The industry has to help itself. What is really needed is a better and deeper understanding amongst banks as to what should be the way out. If the banks take equity risk, they should be compensated with the equity upside. If this concept is clear, they either get in the right kind of management with the right incentives or do whatever is required to resolve the asset. But resolutions have to be found.

Once the accounts are classified, in the first year, 15% provisions will be required; the next year, a further 10%; this will be followed by another 15% in the year after; and the year that follows will need a humongous 60% provision. That will also be the year when Basel III and NDS kick in. Now banks cannot afford to get into such a situation. Therefore they have about 18 to 24 months to ensure that the productive assets are back on track and the problem is resolved.

Ms Bhattacharya didn't think there would be any external help in the form of capital or a 'bad bank'. These ideas have been discussed but have not been endorsed. The solution has to come from within. All banks must work together to resolve the situation. It may not happen very quickly or easily; but it is the need of the hour, and there is no other way.

There is a lot of space for banks to grow in retail. Much of India is in the unorganised sector. Banks must have the right kind of models to lend to them. They must constantly revisit their portfolio and then tweak their underwriting norms to ensure that they don't raise the NPAs. Retail is a high cost model because it is a high-touch activity. Banks must have that high-touch. Public sector banks also need to improve their 'feet on the street' if they wish to ramp up their retail offerings.

She disclosed that the reason why State Bank can move in so many directions and still maintain a steady pace of change is collaboration. The Board and top Management laid out strategies, broke them down into projects, and then delegated the execution of those projects to different teams. There is simultaneous execution on many fronts. Once the people know their goals, they are given the space to innovate and do things themselves. This gives them a sense of purpose and with that comes satisfaction. They have also been able to collaborate across verticals and also with external agencies.

In response to a query about whether in the near future, public banks could introduce agent banking, Ms Bhattacharya said that they already have the franchisee model for the last mile, and that is basically agent banking. Where India has really made a difference is that most of them are enabled on the e-KYC. Once a person is identified, transactions can take place and there is no way of going wrong. But the bank must oversee and retain control over the activities of the agents. They must be properly trained and must comply with all norms. It requires a lot of manpower and technology, but if done well, it is the best way to achieve financial inclusion. In order to assist all customers, most banks have an internal helpline. There are ways for staff to get immediate answers for anything they may not know. They are being trained that not only must they have the knowledge, but they must also know where to get it. "It's like an open book exam," she concluded.

Mr Vishwavir Ahuja

Mr Ahuja discussed the scope that a small player can have in the banking sector, with so many large banks with well-established franchises, huge branch networks and physical infrastructure. Describing his own experience, their institution was built on the basis of the multichannel strategy, drawing upon their direct as well as partnership channels. They partner with other NBFCs, microfinance institutions, e-commerce companies, fintech companies and other distribution partners. They have differentiated themselves from the large public sector banks that have a number of business correspondents, by following a credit-led strategy, rather than targeting opening and servicing of accounts.

Beginning with credit, they go on, through their channels, to payments such as savings and insurance. One reason for their success, Mr Ahuja felt, is that these partnerships are managed "very tightly." He explained that they have 14 corporate BC partnerships and 250 managers who oversee all aspects of governance, compliance, technology and risk management. They have set up a model that enables them to manage these partnerships and keep the whole agenda on track. That is how they have been able to grow.

Mr Pramit Jhaveri

Mr Jhaveri offered a foreign bank's perspective on Indian banking. He was asked whether multinational banks saw India as an attractive market to invest in. Would they again set benchmarks in India for innovation in SME and retail?

He began on a positive note. He felt that "the time has come for us to shift the narrative away from the bad news and think about the opportunities." His bank, he informed, had presence in 103 countries in the world. Unarguably, India represents the top two or three most attractive opportunities in the financial services industry globally. After the global financial crisis, many banks felt the need to go in for radical restructuring. But that did not happen uniformly. Those who underwent restructuring emerged stronger. The others still have "lots of work to do." So now the industry has two different groups of players.

Today, the global economy is short on growth. The banking industry is obviously a derivative of that. So we have a banking industry that is not growing globally and struggling in terms of returns and equity. But if a bank has an efficient operation in a country like India, the returns that can be generated in India are well in excess of the global average.

Going about 20 years back in history, foreign banks were at the forefront of innovation and creativity. That was because they had the intellectual capital to leverage technologies. Today, in a country like India, neither technology nor intellectual capital is a monopoly of any one segment. It is neutral towards who the owner of the bank is. It is a much more level-playing field where everyone has the opportunity to utilise it and succeed in a changing environment.

Mr Jhaveri did not think that foreign banks would operate through wholly-owned subsidiaries in India. When foreign banks went down that route a few years ago, they did that because they wanted a national branch footprint. Today that is not required. Their strategy and outlook have changed. Foreign corporate banks act as a bridge between India and the rest of the world, connecting capital flows. Consumer banking is a little different; there is little merit in trying to compete with a bank that has numerous branches.

Ms Roopa Kudva

As a member of the Banks Board Bureau (BBB), Ms Kudva discussed the options for public sector banks to leverage fintech. She explained that there are three key building blocks which will define digital finance:

1) The use of non-traditional data to make credit assessments: From being a very data-poor country, India is now becoming very data-rich. 'Big data small credit' is the use of non-traditional data to make loans to both underserved retail consumers and small businesses. Today India has 400 million Internet users. Whenever people transact on the social or digital media, they leave a digital footprint. All that data can be leveraged to make credit assessments using intelligent algorithms.

2) The cost of delivery of financial services and discovery is rapidly getting disrupted by the advent of online marketplaces. It is now easier to discover small customers, and costs are being lowered through the transition to paperless lending.

3) The approach towards devising innovative products is very customer-centric.

How do all these building blocks come together? Financial information can be very neatly organised and accessed 24 X 7. Intelligent algorithms can take expert advice, customise products and put them all together in a digital bank.

Specialisation and differentiation are bound to happen. There will be a handful of top-ranking banks which will be full service universal banks; beyond that there will be differentiation. Differentiation could be according to regional concentrations, wholesale, retail, customer segments, industry segments, and digital. Collaboration will be the order of the day. Banks cannot afford to ignore the start-ups. There will be partnerships with start-ups. That is how banks can differentiate their strategies. Public sector banks are very positive in their approach towards experimenting, partnering and innovating.

The BBB is taking a phased approach towards HR issues. The priority at present is to fill up vacancies in the positions of CEO, Chairman, MD and ED. There is also some focus on restructuring. There are a number of issues and they will be tackled sequentially, in a phased manner.

Mr Rajeev Rishi

Central Bank of India, with almost 5000 branches, two thirds of which are in rural and small towns, caters to all types of customers, from big corporate houses to small and marginal farmers. Over the years, they have built a huge loyal customer base. Even if they embrace a differentiated strategy, they will still continue to serve these loyal customer segments. But in the changed landscape, with increasing competition, the arrival of fintech services and more discerning customers, they feel that they must be the preferred banker in some segment where they can outdo the others. Financial inclusion could be one such segment. They opened almost 10 million accounts for the financially excluded. These accounts have now matured and are actually giving the bank business. This could be a good area to establish a niche.

Another niche sector they have identified is the unheralded senior citizens. Twenty per cent of the country's population now belongs to this segment. With increasing life expectancies, the bank could engage with them very meaningfully.

HR issues are a constraint. The bank needs some leeway in recruiting people, and being able to pay more in order to retain talent in areas like risk management and treasury. A lot needs to be done in this area.

Mr Shyam Srinivasan

Mr Srinivasan shared his perspective about the transformation taking place in the banking industry. "A fundamental shift that is happening is that customers are segmenting." That is beginning to defend and dictate banking strategies. Unfortunately, in our country change has to be by stealth. "The moment you mention change, all our guards go up." People feel that something negative is going to happen. Therefore change must be brought about discreetly and allowed to get ingrained into the system.

In a large system, change requires time. It is hampered by frequent change in leadership merely for historical reasons. A certain degree of trust is required, and is fostered when the stakeholders are convinced that the leader is not about to leave or benefit personally. Continuity of leadership has had visible impact on change in the banking sector, especially when large public sector banks are compared with their private sector counterparts who have leaders for 18-20 years. Change cannot be episodic. It has to be ingrained and deep-rooted in the grassroots. That is hard work.

The motto adopted in Federal Bank is 'Digital at the fore but human at the core'. The bank recognises that clients are varied, with many different types of customers. He cited the case of one of their oldest and most crowded branches in a place called Angamaly. Customers have been banking there for generations, over almost half a century. When the bank tried to convert the branch to a largely self-serviced digitally-led operation, the customers protested vociferously. They preferred to wait in a queue for 20 minutes. Banks have to be extremely sensitive to the needs of such clients. Federal Bank is trying a hybrid model which serves both the contemporary customer as well as the more traditional ones.

Mr Ashwani Kumar

Retail has drawn the attention of the banks over the last few years. The market is growing. Mr Kumar did not think there is a systemic risk that should raise alarm bells. In India, 65% of the population is below 35 years and the demand is coming from them. As the GDP grows, the ratio of consumer spending to GDP will also rise. The penetration of retail to GDP is around 9%, in comparison with 23% in China. There is space to grow, and there are avenues to grow. There is no reason to worry about risk. Of course, banks must have proper systems and risk management policies in place.

*(L-R) **Mr. Rahul Jain**, Partner, BCG India, **Mr. M R Umarji**, Consultant, Indian Banks' Association, **Mr. Dinesh Khara,** Managing Director, State Bank of India, **Mr. Rashesh Shah**, Vice President, FICCI and Chairman and CEO, Edelweiss Group, **Mr. Arun Tiwari**, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India, **Ms Zia Mody**, Senior Partner, AZB & Partners.*

Session on 'Resolution and turn around management'

Session moderated by **Mr Rahul Jain**, Partner, The Boston Consulting Group, India.

Panellists

- **Mr Dinesh Kumar Khara**, Managing Director, State Bank of India and ex-CEO and MD of SBI Mutual Funds.
- **Mr Arun Tiwari**, Chairman, FICCI's Banking and Financial Institutions Committee and CMD, Union Bank of India.
- **Mr Rashesh Shah**, Vice President, FICCI and Chairman and CEO, Edelweiss Group.
- **Ms Zia Mody**, Senior Partner, AZB & Partners.
- **Mr M R Umarji**, Consultant, Indian Banks' Association.

Overview by Mr Rahul Jain

This is a subject which is heavily debated. Unfortunately, there are no easy answers. Our panel brings together a slightly more holistic perspective, with representation from the lender, investor and legal fraternities.

Looking at the situation from industry's point of view, there are many positives for the banking industry today; yet, this is an area of concern. Asset quality has fallen over the years. Between 2011 and 2016, stressed assets have more than doubled as share of advances. While there are many factors that contribute to it, there are four core sectors that contribute more than half of the stress: iron and steel; power generation; infrastructure; and textiles. More than 50% of the stressed assets reside within these four sectors.

Attempts have been made to resolve the issue. Measures like corporate debt restructuring (CDR), strategic debt restructuring (SDR), 5/25, and very recently, scheme for sustainable structuring of stressed assets (S4A) have been implemented, but a perfect solution to the problem has still not been found.

CDR has in some ways postponed the problem. There were 44 failed cases, and only 5 successful exits. Hence CDR got morphed into other schemes. SDR, which intended to change the promoter and find a new investor, also got very few successful cases. Promoters began using investors as 'fronts' while actual investors continue to be wary of hidden liabilities and ask for a very high haircut. As a result, there are very few successful SDR cases. 5/25 defers cash liabilities but does not resolve the issue of underlying unsustainable debt. Just after a year or two, there were slippages across multiple accounts. It is too early to comment on S4A but there are some obvious issues that need to be sorted. It factors in only the past and existing cash flows; often this is not sufficient to fit the required EBITDA to furnish the future debt. It also does not allow reworking of the whole payment schedule. As a result, many projects don't fall within the S4A regime.

Recent interventions such as the Insolvency and Bankruptcy Code are steps in the right direction but they will take a few years before they fully come into action. As a result, the current environment continues to be challenged. And it is not just one entity that can solve the problem. It is a multi-stakeholder problem. The entire ecosystem needs to be supported to ensure that a fair working model is found.

Existing lenders are looking to reduce current provisioning. They are compelled to force-fit solutions into standard available schemes. They want a low risk of investigation and don't want to put good money over bad money. Hence credit has risen in this sector, which is bad for the economy.

Potential investors are looking for the correct valuation because they want a fair return on their capital. They are also looking for transparency and corporate governance because they want to be sure that their interests are protected. They want legal and financial protection against liabilities.

Existing owners are obviously seeking time. With time comes hope. They try to defer the issue, hopeful that a solution will come. They want to retain control over businesses which they have built. They also want to safeguard their personal liabilities and guarantees.

These are conflicting interests and finding a solution which marries everybody's interest is not easy. What we need is something that works for every stakeholder. The entire ecosystem needs to gear up to ensure that the solution is holistic.

What we find is that the credit in the corporate sector in general, is quite shallow. There are no investments. This has killed the appetite for risk amongst potential promoters and entrepreneurs. Nobody is willing to take large projects today. If the economy has to grow, the four core sectors mentioned above have to develop; unless adequate credit flows there, the economy could get completely paralysed. So we are at a standstill.

The measures that are being taken are too slow to have realistic solutions in the short term. The quantum of stress is very high. It requires significant focus and intervention to resolve. The sectors impacted are core to the Indian economy. Credit control is not a long-term viable option. The situation has reached a stalemate with no visible solution. All stakeholders need to work together to find a holistic solution and take steps in the right direction.

It is not the banking fraternity which is to blame for the situation. It is a much broader problem which encompasses all elements of the economy. Everybody is painted with the same brush. There is no differentiation between promoters, between repeat and first-time offenders, between those who have been fair and those who have not. The effort of setting up and operating a business in India is not well recognised. Most of the resolution schemes, especially SDR, have been aimed at taking away management control. Industry has been running in search of investors without genuine intent or ability. They are now worried about legal action. In the process, business is suffering. Working capital has got squeezed. Credit control in the economy has had a ripple effect; and today, nobody is interested in longer projects. As a result, even completely viable projects that are halfway complete are looked at with suspicion. There is a trust deficit in the system. Currently, no lender is willing to investigate or even evaluate projects which have high viability.

There is no easy solution; patience is going to be tested. The times ahead are going to be tough because more difficult decisions will have to be made company by company. What is needed is a solution that works for all the three stakeholders — existing lenders, existing owners and potential investors. A solution that is commercially viable for everyone needs to be created. The governance mechanism should facilitate creation of the right environment for all types of investors to come in and get a fair share of the upside on their investments. This will be a step in the right direction.

"Why is this not getting administered?" Firstly, observed Mr Jain, there are limited options for timely intervention. By the time banks get to know about it, it is too late before reality hits. Secondly, there are very limited avenues for early exit. Even if the bank decides to exit early, the opportunities are not there. The most critical issue is that swift decision-making and execution are very difficult. Coordination amongst banks is a challenge. "There is a lot of fear of CVC and all kinds of questioning after a few years. Nobody wants to take exceptional decisions." Banks are really not empowered to pin point the solution. Historically, options like BIFR are used by the promoters as a stalemate. "The Insolvency and Bankruptcy Code is hopefully a step in the right direction," Mr Jain said.

The focus is on provisioning and not on long term recovery. It is only when the problem becomes large that they actually start solving it. He shared some interesting learnings about how other countries have dealt with this. Different solutions were tried in different countries over the last couple of decades. In Europe, a few countries like Spain created a 'bad bank'. It is a bank which is equipped to deal with stressed assets. "They pooled in all stressed assets across banks into one entity and they created the right capability and authority levels to deal with the problem," he explained. South Korea created a strong government-backed AMC which was asked to buy out the debt across banks at a certain term, and then deal with the problem in the right way with the longer-term intent to solve the issues with the right competencies. China created four or five large state-owned AMCs and took over the bad debts from the banks at a certain rate. They then ran the turnaround successfully; today these AMCs are actually investing in overseas stressed assets.

The underlying problem, he reiterated, is "coordination and decision-making, alleviating CVC fear and getting the right decision at the right time." One extreme view is that ownership solutions or central asset solutions should be created. On the other hand, there is optimism "that we are moving in the right direction." In this catch 22 situation, the focus on business moves away. In trying to resolve the financial issues, there is significant damage to business. Unfortunately, there are no standard solutions.

Panellists' Views

Mr Arun Tiwari

"All bad loans are underwritten in the good times of the economy," declared Mr Tiwari. During the economic boom about 10 years ago, somebody who was a trader became a manufacturer; somebody working for a big firm became its promoter and was helped by the manufacturer and by the banks as lenders. All this was done in the name of entrepreneurship. Capacities went up and the economy soared. Then came the downturn. Now nobody has the answer. The lenders are asked when the stress will reduce. Mr Tiwari's riposte to that was, "give me a date when the economy will pick up on a sustainable basis, keep us six months behind that and it will all be okay."

The economic downturn came with the capacity expansion. Why did the capacities go up? Because it was the economy's demand. The Government wanted banks, especially the public sector banks, to help the entrepreneurs and industry in general. Bankers then became sleeping partners. But ultimately, bankers are in the business of banking and not running enterprises.

Everybody looks at the bankers to solve the problem. Banks are expected to take the haircut. "Why can't there be a haircut in the tax collection also?" demanded Mr Tiwari.

In response to Mr Jain's question on who can be considered a good promoter, Mr Tiwari said that a good promoter is one who continues to commit in the business enterprise. It is not easy to find new promoters in sectors like steel, iron, power, textiles and roads, which have high NPAs. Professionals may be brought in to manage these sectors; they will have the skill sets but not the risk capital. That is the paradox. Those promoters who have it in their DNA to run the businesses are more willing to come around than first timers. The response of new promoters, whether traders-turned-manufacturers or ARCs, has been dull.

The first round of restructuring was more cosmetic in nature. It was a learning process. There were no whistleblowers who came forward to reveal that a project actually had a much longer life than what was reported; bankers tried to squeeze in cash flows for a much shorter time frame. Such projects were bound to fail. Lenders who supported projects that they felt had economic value were hounded five years later. But still, if a project has economic value and the promoters are on board, banks will be willing to support it. With hindsight, bankers have become more cautious about documenting their actions.

There is also the problem of coordination. Public sector banks are asked to decide the future course of action. But they have two regulators — RBI and DFS. There are many stakeholders. The process is not working seamlessly. Bankers may be catalysts but not drivers. He called for some mechanism to address this. The problem has now become so huge, that a solution in the next few months will not be possible. It will have to be tested. Drastic measures will not work.

Mr Dinesh Kumar Khara

Mr Khara pointed out that the business risk stays with the promoter. As far as the banks and financial institutions are concerned, they are actually putting a stake on the promoter and his comfort and confidence into the risk which they are assuming. "Unless an atmosphere is created where all stakeholders have confidence that there is going to be a fair deal, things will not move ahead," he felt.

Where an asset is already impaired, to think in terms of additional funding letters is a very difficult question for any banker. "Nevertheless, we have to be mindful of two facts," he noted. Leverage is quite high; and a situation has to be created for equity to be there. He observed that there is huge demand, particularly from global investors who are yield chasers. They are looking at opportunities in India, but also want a credible system that can take care of their interests. If that kind of atmosphere can be created here, such investors may be willing to put in money. Hence the need is to create an ecosystem which gives them support and comfort. With that, it may be possible to take care of the interests of the lenders, borrowers and investors.

Confidence of banks in the Joint Lenders Forum is extremely important to enhance coordination. Equity must be built-in into this kind of structure with a mechanism that engineers trust. The operational guidelines should be of benefit to all concerned. Trust will help coordination and also decision-making.

Structural issues such as enabling legislation have been addressed. As regards the stock of the accounts with the ARC, unless there is a resolution component on the ground which can actually turn around those assets, the ability of the ARC to produce more accounts will be impaired. The right people are required who can be put in the companies so that they turn around and start generating cash for the benefit of the economy. A cadre of 'insolvency professionals' will be of immense value. At the same time, banks will have to create capacity which can deal with such stressed situations; they have not confronted such situations in the past. He suggested that in due course, the Institute of Banking and Finance can come up with structured courses that can give the required skills to the bank cadre on dealing with such situations.

Ms Zia Mody

With so many stakeholders, said Ms Mody, promoters may wonder why at all they are working for the bank if the equity is seen to be zero and they get nothing. Banks still need to find ways to incentivise the promoter. "How do you get the promoter to put in more skin in the game?" He has to believe that he gets something out of it, she stated. Banks have to accept that. If they want a good situation for themselves, the promoter has to be benefitted in a transparent manner.

There is also the question of getting senior bank officers to agree to a proposal which may have some risk, without the threat of being hauled up by the CVC, CBI or bank board at a later stage. Investors may put in a certain amount, and the funding gap will have to be covered. Ultimately, the Government has to find the capital shortfall. Promoters have now come to realise that they cannot defer the problem indefinitely. That time has gone for the banks. The revival schemes are work-in-progress. The issue is how much haircut can the banks take, and how much of their haircut can be passed on to the promoter who actually caused the haircut to happen.

One of the things that will happen in the next five to ten years is that there will be reliance on professionals who can actually turn around the company. They are present in India today, and their breed is growing. They can reduce the banks' reliance on the promoter from a professional management point of view. The expertise of the promoter can then be used in pockets where the workout team can use it to the best extent. "I think that the new landscape is going to consist of insolvency professionals where the rules are being written up," Ms Mody predicted. But the Insolvency Act "has got a sword which doesn't give you more time." She asked further, "It is all very well to say you will be automatically liquidated. What does that mean to workers, to suppliers, to vendors and how many private liquidators are you going to get into the Indian system?" Her suggestion to banks was that they should start building ties with other professionals who could help them in such a situation. Such professionals may be able to minimise losses and try and stabilise operations.

Mr Rashesh Shah

There is no homogeneity amongst promoters, but ultimately economics has to be the primary driver. Whether to continue with the current management team has to be decided on the basis of economics. It should not be seen as management control being taken away. There is a process by which the economics of the upside will be shared by the promoters and management, the bankers, and the new investors. The promoters want to maintain as much upside as they can; the banks want to take as little a haircut as possible; and the investors want a good return on a risk-adjusted basis. Currently this process has broken down. The new Bankruptcy Code may allow the process to go through smoothly. How we resolve the issue will be important.

Banks should not be made to give additional funding. That should be accessed from other sources. This will actually validate the revival ability of the restructuring package. Once an asset is impaired, if anybody gives it additional funding, that is truly high-risk. A structure needs to be built around that. There is what is called a 'priority loan'. RBI has been speaking about creating a 'super senior priority loan' which goes in and then comes out first at a reasonable rate of returns. If that structure can be put in and insulated from the impairment of the old asset, the existing banks as well as quite a few NBFCs and other funds may be happy to fund the project. Then the only problem will be about assessing whether the asset can be restructured. Additional funding will not be the problem.

Speaking from the point of view of an ARC, Mr Shah disclosed that his company spent over a year just aggregating debt. This takes a lot of effort. Without it, restructuring or additional funding cannot take place. They would like all sales to take place through a consortium process; but unfortunately each bank has its own priorities. The approach then becomes diffused. He was of the view that when an asset is going bad, it is important to act quickly through a consortium-based approach. Currently, banks still have to go back to their own boards and get the decision approved and ratified. This takes a long time. If a decision is taken at the consortium level, enforcement and follow through become automatic.

In his experience, unless financial restructuring is first carried out, operational restructuring cannot be done. ARCs have largely focused on financial restructuring but still there are issues. If those issues can be got out of the way and then skilled management brought in, an operating turnaround can be done. It is not an 'either-or' situation. Financial restructuring has to be done before an operating turnaround can be achieved. The former will need to be done largely through the Insolvency Code.

It takes about a year-and-a-half to aggregate debt, complete the financial restructuring, get in additional liquidity, and then agree on how the equity will be shared. At the end of the day, even though banks see themselves as mere credit providers, they actually create equity value. It is important not to confuse equity ownership as a financial decision with ownership over control of the company. Equity ownership is only a financial decision. Banks can own 80% of a company and still not be operating owners of the company.

A lot of NPAs are revivable. There are a whole category of companies which are EBITDA positive but not cash flow positive. The EBITDA is not enough to service interest and repay their loans. If part of the loan can be converted to equity, the asset can be made a lot more revivable. Many of such projects need just the last mile funding. For example, a commercial mall has no economic value even if it is 80% complete, because it can't earn anything. But once completed, it gets economic value. There are many such projects that can come back on track.

Mr M R Umarji

Financing a stressed unit is a major issue. Public sector banks are reluctant to take decisions on such issues. The jurisdiction of the CBI and CVC becomes applicable because public sector banks are owned and controlled by the Central Government. The employees and the officers of the bank become public servants for the purpose of the Prevention of Corruption Act. Mr Umarji suggested that "there is one solution for this entire problem to enable public sector banks to function as any other private sector bank." His idea was that they can be converted into companies. Once that is done, they will have the freedom to take whatever decisions they want without being questioned by the authorities at a future date. The shareholding of the Government can be reduced from 51% to 49%. Once that shareholding is reduced, the banks will cease to be under the authority of the state and will not be subject to the jurisdiction of the CVC and CBI. That will solve the problem, and also address other issues relating to HR. Public sector banks are bound to uphold fundamental rights and cannot deny equality of opportunity to any person. They can be questioned if they select candidates from an institute of management because that is considered discriminatory. This problem will not be solved unless the structure of the public sector banks itself is changed.

Banks may, at some stage, end up being owners of companies. They will need to consider the provisions of the Insolvency Code to ensure that they have the right ecosystem to help them manage the business. If an entity commits a default, an insolvency petition can be filed against it. If the default is confirmed, the court will have to pass an order for the insolvency resolution process. Once the insolvency resolution order is passed, an insolvency practitioner is appointed. He has to take possession of all the assets, and take over management of the company and run it. To create the capabilities for doing this kind of exercise is a major challenge. In fact, it will be a stumbling block; those who cannot do it will not go to the insolvency court.

The bankruptcy laws of the United States and some other countries have the concept of a debtor in possession. That concept is not provided for in our Insolvency Code. Hence the bank itself has to take possession through the insolvency practitioner, and manage the show.

But there is another solution: the promoter can proactively inform the bank about the problem. That way, the company can try to start working out a scheme for revival. Banks will have greater confidence in somebody who levels with them about his difficulties; some possible arrangement can then be worked out whereby the insolvency practitioner, who will run the business as a going concern, is appointed with the consent of the promoter as well as the bank.

Special Address on

'Banking Horizons: Clouds And Silver Linings' By Shri S S Mundra, Deputy Governor, Reserve Bank of India

"This seminar has become a very important event on the annual banking calendar," began Mr Mundra. He pointed out that just like last year, the Governor spoke in the morning and he in the afternoon; so there was bound to be some repetition. "But the repetition underscores two very important things," he emphasised. "One, there is uniform thinking as far as RBI is concerned. All of us think and speak in the same way. And the second, very important point is that truth will always be the same. You need not invent it, whether it is the Governor, or I, or any other colleague of mine speaking."

Every day, the world has to deal with a new event, he continued, citing examples such as Brexit, or the crisis brewing in the Italian banking system. The scenario is very fluid. Global economic recovery with several revisions by the IMF still looks hesitant. IMF estimates the global growth for 2016 at 3.1%, and for 2017 at 3.4%. The growth in advanced economies appears almost flat at 1.8%. In the emerging economies, growth is expected to be 4.1% in 2016 and 4.6% in 2017. Ultra-loose or ultra-accommodative monetary policies and negative rates of interest may have conflicting consequences. For example, if the Fed raises the rate, but at the same time many other advanced economies announce accommodative policies, it is not clear what the combined impact will be. This lies in the realm of uncertainty.

Globally, regulation is becoming more intrusive. It is of concern to India, as an emerging economy, that in addition to the common agreed minimum international rules, there are countries that impose their own regulations. Two points that are under serious debate are: (i) whether sovereign debt should be entirely risk-free or it should have a risk weightage; and (ii) whether there is need to bring in a new standardised approach to apply risk weight for credit as well as operational risk under Basel III. Where are these concerns stemming from? In the case of sovereign debt, many countries have raised sovereign debt in currencies that are not their own, with instances of default. As far as credit risk is concerned, there is no uniformity in applying risk weight. If any of these two points is adopted, it will impact capital requirement, profitability, and raise many other issues. In a year's time, India will move to the new accounting standard which will have its own requirements regarding capital, provisioning, asset recognition, etc. This will impact the banks' profitability, and may be of concern to the regulators.

Sovereign debt or change in risk weight can have implications on capital adequacy. "As a regulator, we need to be worried about the banks' profitability because profits and internal retention are the major source of capital creation in any bank." Capital is very important for banks to be able to continue their lending activities. Banks in turn are important for the real economy; hence it is important that they get a decent return on the capital that they employ. Emerging markets like India have been advocating that while the regulations may be fine-tuned, they should not demand significant additional capital from their banking systems. But in any international forum, with several countries and several very distinct groups, there could be interests which are not aligned with each other. We need to be aware of the possibilities and be prepared for that.

The NPA crisis has been the most discussed topic in the banking industry over the last one year. There are still components which need to be addressed. Mr Mundra referred to a report released by an investment advisory that indicated that the interplay between NPA and structured assets was relatively reduced in the current quarter. He explained that if there is a 100 basis point migration, the interplay between NPA and restructured assets is only 30 basis points. This implies that 70 basis point stress has come from fresh sources. Two trends become quite clear: there is moderation in the accretion of further NPAs; and most of the banks have reflected much better recovery performance. But the need for provisioning will continue because of the fresh accretions and the ageing of old NPAs.

"Resolution can't be delegated," said Mr Mundra. Once a particular structure is adopted, resolution cannot be delegated at three levels:

Firstly, the whole resolution planning cannot be delegated to any outside agency. Assistance may be sought from them, but not complete resolution planning. Secondly, if a group of bankers is involved, delegation cannot be done to one or two banks. All players have to be active partners in making that resolution successful. Thirdly, when a resolution planning group meeting is held, participation by very junior officials does not lead to any conclusion. The resolution group should be represented by senior management and whatever decision is taken should be implemented very quickly.

The banking industry has spent a lot of time and energy in tackling the large corporates; but the other part of the portfolio i.e. retail or agricultural or SME loans also needs attention. These segments have their own challenges. The credit growth rate for the year ended March 2016 shows a clear divergence between two segments in the banking industry. One segment shows credit growth of over 20%, and the other is at 7% or 8%. In Mr Mundra's view, some of this difference stems from cherry picking migration of credit from one segment to the other. The industry that is losing credit in that manner should be conscious that if they fail to retain their existing business, their residual portfolio will not be very comforting.

It is widely known that a majority of corporates have an interest coverage ratio of less than 1. At the same time, the RBI has issued certain papers; one of them is about the changes which are proposed to be brought under the single borrower and group exposure limits in order to harmonize our regulations with international regulations. Another discussion paper outlines the roadmap that RBI proposes to follow in migrating some corporate credit to the market when it exceeds a certain limit. This provides an opportunity for banks to assess their individual portfolios and rebalance as required. As far as MSMEs are concerned, 78% of them still source their credit from the informal market or their own sources. This means that there is lot of scope as far as MSMEs are concerned. There is also a lot of scope in retail with urbanisation and the rising middle class. Retail and MSME have now become the fashion statement of the time.

But it is not as simple as that, cautioned Mr Mundra. "If you enter into a sector without proper understanding and sufficient back office preparation, then these things come back to haunt you at some point of time in the future." MSME and retail may have the potential but it is very important to understand the business and have robust back office preparedness. Both these segments need accredited credit counsellors because MSMEs face a challenge in approaching the banking system. He disclosed that RBI has already initiated some work in this direction.

The agricultural banking industry is setting higher targets year by year, which are being accepted and achieved. But there will be a limit. Unless the credit absorption capacity of this sector shows improvement, it could be risky. Credit absorption capacity may come from land reforms, investment, creating a proper ecosystem, and ensuring that there is an effective insurance scheme. When all that is in place, this sector will have a larger credit absorption capacity; that will be the time when continuous increase in agricultural lending will be sustainable.

Some banks have taken the initiative to become more competitive. NBFCs and MFIs have better last mile connectivity, with a more intense and direct connect with customers. Banks have a better capital and funding availability. "Is there a possibility that these two capabilities are leveraged by coming together?" asked Mr Mundra. He was referring to joint origination where each single loan is jointly originated. The loan amount is shared in a certain percentage, risks and collections are shared, and there is a fair agreement about the rate of interest and the fee for the additional services that one of the partners would be putting in the structure.

Mr Mundra expressed concern that there were numerous instances of mis-selling, particularly mis-selling of third party products. The RBI has asked banks to institute the office of internal ombudsman. He emphasised that this is an area of deep concern. If no perceptible improvement was seen, or if instances of mis-selling still appeared, the consequences would be quite serious, including levy of a financial penalty. Banks have the responsibility that their customers get a fair deal and are not misled by the dealing staff. But he was not convinced that the mis-selling occurred due to individual action; rather he felt that individuals are guided by some broader performance pressures that are imposed on them. If there is a doubt between an institution and individual, the benefit of doubt will undoubtedly be given to the individual.

Account number portability should be possible with the UPI. If mobile numbers can be portable, why can't account numbers be, Mr Mundra wondered. "If the account number is portable, then no customer will suffer in silence." They will migrate their business without losing connectivity and data. This is very much a reality with UPI and is a wakeup call for the banking system.

The RBI has taken a lot of initiative on account opening in recent times. Mr Mundra observed that financial illiteracy is not only on the customer side, it is as prevalent among the banking staff. At times the customer may be aware of the requirements for account opening, but the branch staff insist that they are not sufficient and very often they put the onus on the RBI. The customer has no way to dispute it. Hence RBI is publishing simple small points which the customer can take to the banker.

Mr Mundra also referred to cases of cyber fraud. Most instances were known cases but one new element noted in the recent past is cases of fraud in documentary credit, such as fake LCs in connivance with the bank staff. It is very important to monitor what is actually happening in these accounts. He felt that post monitoring of accounts is lax and that is why there have been instances of money muling. He called for a strong central surveillance system for transactions in the account, and a strong central processing system for documentary credit.

He was clear that all this requires a long-term vision and continuity of effort. When leadership changes are frequent, such long-term plans may not be followed. This is something for the boards of banks to ponder over. He cited the policy of the Monitory Authority of Singapore that for any new innovation, the regulator would apply the test of materiality and proportionality. The regulator would enter the picture when it felt that the risk was becoming material, and not try to stifle the innovation at the very initial stage.

The time has come that in some areas, banks can pool their resources, in the manner that HSBC and Morgan Stanley are coming together to share back office technology. He said that he would only be worried if trading and fee generation become more important than lending. "The core dharma of the banking system is lending and all other activities should be second to it." As regards HR and governance, he simply quoted a message from the G30 Report: 'The board and the senior management need to make sure that the voices of the middle management and the echo from the bottom can be heard'. He concluded with the assurance that "silver linings are not elsewhere, they are always at the edge of clouds only. The need is to discover them and act on them."

(L-R) ***Mr. Ruchin Goyal****, Partner, BCG India,* ***Mr. Satish Pillai****, Managing Director & CEO, CIBIL,* ***Mr. V Srinivasan****, Deputy Managing Director, Axis Bank,* ***Mr. Rajnish Kumar****, Managing Director (National Banking Group), State Bank of India,* ***Ms Zarin Daruwala****, CEO – India, Standard Chartered Bank,* ***Mr. Abhishek Bhattacharya****, Co-Head – Banks and Financial Institutions, India Ratings and Research,* ***Mr. Vikrant Chowdhary****, Head - BFSI and Telecom, SAP Indian Subcontinent,* ***Mr. Ajay Pandey****, MD and Group CEO, GIFT City.*

Session on 'New ways to do credit and monitoring in the new age world'

Session moderated by **Mr Ruchin Goyal**, Partner, The Boston Consulting Group, India.

Panellists

- **Mr Rajnish Kumar**, Managing Director (National Banking Group), State Bank of India.
- **Ms Zarin Daruwala**, CEO – India, Standard Chartered Bank.
- **Mr V Srinivasan**, Deputy Managing Director, Axis Bank.
- **Mr Satish Pillai**, Managing Director & CEO, CIBIL.
- **Mr Ajay Pandey**, MD and Group CEO, GIFT City.
- **Mr Abhishek Bhattacharya**, Co-Head – Banks and Financial Institutions, India Ratings and Research.
- **Mr Vikrant Chowdhary**, Head - BFSI and Telecom, SAP Indian Subcontinent

Overview by Mr Ruchin Goyal

"There has been a marked slowdown in the credit growth in India," began Mr Goyal. Over the last 15 years, the credit growth in India has been between 15% and 30%, growing at about 2X to 3X the rate of growth of GDP. But over the last two years it has come down to single digit numbers. It is also common knowledge that NPAs are rising. Yet, if we de-average the NPA numbers, there is one silver lining. That is in retail loans. Other sectors can learn from this: in the early 2000s, when a lot of retail started happening in India, there was very little data available and a lot of institutions burnt their fingers while doing retail credit. A lot has changed over the last 15 years. The Credit Bureau has now become a very powerful source of information for banks. Banks, in turn have developed risk models for retail customers, with much better prediction capability. What will it take for the same to happen to MSMEs and corporates?

There is still under-penetration in terms of overall retail loans in India. Taking the case of mortgages as an overall percentage of GDP, it is 9% in India, and anywhere from 15% to 25% in similar markets in Asia. It is substantially higher in the developed markets. If India's mortgage penetration were to achieve the levels of other Asian markets, retail loans and mortgages will continue to grow at 2X or 3X the GDP over the next 5-10 years.

MSME is another very under-penetrated sector. About 78% of MSMEs actually use informal sources of credit. The MSME sector has been growing at only 12% over the last 20 years, while agriculture, retail and large corporates grew between 18-20%. This is not because MSMEs don't require credit. It is because banks are unable to give loans to MSMEs.

He asked, "What would it take for banks to lend to MSMEs?" The answer is not simple because there are several challenges. India is still a very large, unorganised economy. The unorganised workforce in India is about 40% in non-agricultural sectors, against 15% in China. Agriculture is almost 100% unorganised. And 50% of the population is in agriculture. These people cannot produce a document which banks can use to lend money.

An example of what can happen when there is credible security and a latent demand in the economy is gold loans. Gold loans have boomed in India at a compounded annual rate of 50% over the last several years. So if there is credible security, which in this case is gold, there is a lot of latent demand for credit. Mr Goyal argued that going forward, banks or financial institutions don't need to take gold physically from customers; they can just use data. "Can data be the next gold?" he asked.

India is at the cusp of massive digital disruption. An unprecedented scale of digital infrastructure is being created. If GST gets implemented, a lot of value chains will have to get digitised. About 3.5 billion invoices will get digitised, which is a very rich source of data for the banks. UPI can be quite a game changer in terms of peer-to-peer payments. Many different industries have completely switched to digital. Customers are ready. India is moving away from a data-poor country to a data-rich country.

The way banking is done in a data-poor country is very different from the way it is done in a data-rich environment. A data-poor environment relies on physical judgement, on the ability of the branch manager to understand the customer, and on local knowledge to take a decision. A data-rich environment makes use of analytics and models to take the same decision.

This has given rise to a large number of start-ups in the fintech space. In 2015, there were 174 fintechs that were established in India. Mr Goyal posed a question for the panel: "Do you think fintechs are enemies that will compete with banks or are they potential partners that banks can partner with and serve the customer better?"

The way business is being done is changing quite dramatically. Agriculture, transport and retail are cases in point. Traditionally they have all been fragmented industries comprising small farmers, small individuals who drive taxis or small mom and pop kirana stores. These were fragmented entities and it was very difficult for banks to reach out to them. All these three sectors are getting organised. In agriculture, there is a rise in contract farming. It is well-known what the Olas and Ubers have done to the taxi segment. The retail story is similar, with Amazon and Flipkart.

Under such an ecosystem, banks have access to data that is very rich, and can connect with the same customers in a more digital manner. With so much data on hand, banks can start forging tie-ups with companies that directly deal with farmers or even the entire supply chain. Once such tie-ups are effected, banks can start designing solutions that are tailor-made for a particular industry. The entire operating model can become digital and dramatically reduce the costs, and also the risks. A lot of rich information can be accessed from the corporates on an ongoing basis, and this information can be used for smart monitoring. This is not done today, but it is the way business can be done, going forward.

Panellists' Views

Mr Rajnish Kumar

The way business is being done is undergoing a massive transformation due to digital disruption. Banks have to keep pace with the times. State Bank of India has tied up with many e-commerce players with new financing models that include partnerships, technology, and the use of data analytics. The organisational structure to handle loans has also undergone a change. Earlier, all business was happening in the branches and was controlled by the regional manager or the DGMs. Now loans are sanctioned at a centralised place. The role of the branch is now limited to getting together the documentation. As of now, wet signatures are still required and the branch plays a very important role in loan recovery. Mr Kumar expressed satisfaction with the new system.

He felt that going forward, business volumes should improve. There may be initial losses but such things must be provided for when something new is attempted. Initially, the results may not be very encouraging; even delinquencies may be higher. But the effort will not succeed if banks go into their shell because of this. "Immediate results are never visible when you are starting something new," he observed. It is very important that while entering into this space, the risk framework, risk appetite and expectation on risk adjusted return on capital have to be very clearly defined.

Responding to a query about what banks can do different to identify early stress and catch fraud, he replied that as the loan amount increases, the intensity of the relationship has to increase. The major problem with corporates is capturing the cash flows. It is not humanly possible for a relationship manager or credit analyst to scrutinise all the accounts; now with technology, the exceptions can be identified and analysed. The biggest comfort to a lender is that these electronic platforms can capture cash flows. But human intervention cannot be eliminated when dealing with credit. " I don't foresee in future that particularly when it comes to corporate credit, you can do away with intelligence despite so much data being available." Technology becomes much more effective in small loans and large volumes.

Ms Zarin Daruwala

Ms Daruwala was asked about fintechs. Are they partners or competitors? "I would say a bit of both," she replied. Today the world is seeing the 'Uberisation' of banking. 'Uber' is now a word which is used to symbolise radical disruption of an industry. Uber is the largest taxi company owning no vehicles; Facebook is the most popular media company, creating no content; Alibaba is the most valuable retailer, having no inventory; Airbnb is the largest accommodation provider, owning no real estate. The banking scene is similar. Banks have legacy systems which are not easy to change; fintech companies can start with zero base technology models. The latter can be great disruptors. The KYC and ALM norms in banks are much regulated. The kind of KYC that a fintech company has to do is very different from what banks have to do. They have an edge over banks in small value transactions.

Banks can partner with fintech companies because they help in two fronts: reducing the cost to serve; and reaching out to the largest segment of the population. This can really help banks, especially those that don't have a large bank branch presence. So fintechs are partners-cum-competitors for banks.

While banks are using analytics in a big way on the retail side, they are not using the same kind of analytics on the corporate side. It is very easy to use technology to figure out whether money is moving from the corporates to the promoters' investments company. Circular transactions can be identified. There are many ways in which technology can be used to find out what is happening in the bank. The banking community should come together and focus on how to use digitised government records and databases to examine whether the finances of a company are a true representation of what they state. If banks sharpen the way they have been doing monitoring, technology can be a big enabler.

Mr V Srinivasan

Banks need to fo cus on two aspects to leverage their potential. One is the people aspect, and the other the technology aspect.

People have been used to a certain way of doing business. They will experience the value of how business analytics and data change the way business can be done, and help in decision making and improving efficiencies over a period of time. It is important to start early, in small pockets, grow it and let people start believing in it.

Speaking about the technology aspect, Mr Srinivasan felt that the effort required to set up the internal infrastructure is quite massive. It involves a lot of lead time. Sometimes the banks have disparate systems, with various products in different systems. All of them have to be brought together to get a single source of truth. It takes a huge effort to build a data warehouse where all the data is in decipherable form. But it is the number one prerequisite that banks need to put in place before leveraging technology and data.

Both these aspects are extremely important. Just having the infrastructure without the people believing in the technology will not work. Likewise, people believing in technology without the infrastructure will also not work. Both these aspects are essential prerequisites for leveraging technology and data for monitoring credit.

He described his experience of corporates and SMEs using digital channels, compared to retail customers. "It is still lot more nascent," he said. Sometimes the documentation aspects prevent the corporates from going digital. But banks have invested a lot in technology to make sure that their products are offered through portals through which corporates can transact electronically. As long as that data is captured electronically, the ability to mine that data to understand corporate behaviour becomes easier.

Everybody is concerned about understanding just cash flows. But ultimately capital structure is equally important. So banks have a lot to do together to create the infrastructure. The biggest game changer as far as banks are concerned is the CRILC that RBI has put in place. This is a single source of truth that will help banks understand what the debt of the corporate is. In his opinion, the next step will be collating the cash flows and making sure that banks across the various accounts understand how the cash flows are moving. Capital structure is also important and very critical in long-term financing; but in terms of the operating aspects related to a company, cash flows become a lot more critical. Both mechanisms need to be in place in order to get a right handle on the credit.

Mr Vikrant Chowdhary

Mr Chowdhary discussed where banks have done well in adopting technology and what they can do better. Over the past two decades in India, the first priority was growth, and the second cost and efficiency. Prosperity came under cost and operational efficiency. The third priority was risk containment and regulatory compliance. This was before automation. Because we are a growth economy, we started with automating for scale. The banking industry grew by automating and standardising the backend for scale. Innovation at the front end and integration of the ecosystem still remain to be done.

The customer experience will become seamless when product-led divisions, such as lending, credit card, core banking, loan origination etc. become seamless and get harmonised at the front. Front end innovation, which is the normal channel from a technology point of view, has not achieved that level of scale.

Integration is no more a choice. Banks will need something like 'API-fication'. The venues of lending will completely change and will become more and more digital.

The architecture of the future will no more be applications to scale. That will happen; but the whole banking system will have technology platform capability and will be able to network inside and outside of the banking system. In the new digital ecosystem, under the hood of hyper connectivity, real time analytics, artificial intelligence, machine learning and blockchains, pieces of technology will find the right usage and the right applications. Credit has so far been a pull product; corporates and individuals come to seek credit for a need. Technology has an ability to change this to a push product which will be consumed as an API. On the monitoring side, technological capability has leapfrogged in terms of likely default and potential NPAs. So a pull product can be changed to a completely push product to be consumed on various forums.

Mr Ajay Pandey

GIFT is a platform which can be used by various banks for doing businesses that they are not able to do today in India. Some of the overseas transactions can be done in India, and there are various enabling regulations that help banks to do them. Such transactions can be external commercial borrowings, or buyers' credit, or organising loans for joint ventures in other countries.

Mr Pandey explained how all this is related to the subject being discussed. GIFT, he said, is a perfect example of a platform where the ecosystem is being generated. A couple of banks have chosen to house their businesses there because of a smart infrastructure as well as smart technology. He revealed that one of the data centres that they host is linked to the largest submarine cable capacity in the world.

All this requires tremendous support at the backend. They are creating a platform where all of this can be supported both from a technology and a people perspective. GIFT is a place where a lot of banking elements are falling in place both in terms of people, technology and processes. They also have special incubation platforms where MSMEs can be groomed, with leads to funders who can engage with them. It challenges the way the market is evolving today in terms of platforms, processes or even technologies.

Mr Satish Pillai

Mr Pillai disclosed that CIBIL has got big data and information about 220 million consumers, 60 million microfinance borrowers, and 10 million companies. "But," he said, "we are still on the path to become a big data company." Turning big data into big insights is a different matter altogether, he explained.

"We have got 60 million loans against gold given every quarter in India." The reason for that, he said is because there is a latent demand; but, the important point is, there is also a process. The consumers go for the loan when they have gold because they understand the process much better than actually going for an unsecured personal loan or a line of credit. It might take 30 days to get a line of credit; it will take 30 seconds or 30 minutes to get a loan against gold. That is powerful when they believe that they can get the asset back.

The big worry for a credit bureau, when underwriting SMEs, is about the credit information of those entities. What happens to those who don't have credit? That problem is encountered through retail all the time. If the credit score or credit history of the individual is available, then it is worth the time and effort to change the process. If there is even one person who could have got a loan that he didn't get earlier because of lack of credit information, that becomes even more powerful.

Underwriting a small business is complicated because of the asymmetry of information, and a lot of data that cannot be trusted. But fintech companies are doing it. They don't have the challenges that a large bank has. From the business standpoint, there are lot of things that banks will not be able to change in the near term about small business underwriting because of legacy issues. However, there are probably two or three things that can be changed, particularly how they use the data, analytics and technology. It is important to identify the processes that can be changed, along with any partners, to be able to solve even 10% or 20% of the problem that exists with SME lending. Mr Pillai was confident that the transformation will happen.

But, he added, "Data and technology does not and cannot replace people." Technology does not give insights; people do. Especially as ticket sizes get larger, institutional knowledge is needed, much more than what technology can do. All that technology can do is to make the process a little easier. The human element is important. There are a lot of skill sets available in India, but from the technology standpoint, the data must be delivered in a meaningful fashion. What is critical is how the technology is used to deliver solutions in real time. The way to do this is to marry technology and data in such a way that the process gets simplified from the customer's point of view, but still offers a lot of comfort from a risk control point of view.

Mr Abhishek Bhattacharya

Mr Bhattacharya considered the lessons that could be learnt from the last cycle. He said that considering the way the loan covenants are designed and enforced, it is monitoring and enforcement that has been an issue. IT can help banks be closer to cash flows. Project costs can be monitored, group structures can be examined more closely while lending and banks can determine whether debt is being repayed from business cash flows or non-operational funds. IT and data can also play a very big role in tracking the forex impact for a company.

Many times the penal fee charged may not be enough of a deterrent. In certain other geographies, all covenant breaches have to be reported as part of regulatory disclosures. Covenants can be used as a tool to negotiate terms better. Other aspects like receivables accounting and ascertaining whether the haircuts involved are realistic will also help in dealing with large corporate stress.

Over the last 10 years all banks together would have added about 80 million customers. MFIs and SFBs together would have added 30 million customers over the last five years. On the one hand, the private sector and large public sector banks look at well-banked customers using real time analytics, and trying to improve their cross-sell ratios. On the other hand there are these other companies who are still creating data, and who are fast growing. They could be very small NFBCs, some even having SFB licenses. They are creating credit benchmarks and slowly expanding. They are creating those benchmarks, and moving from geography to geography before they attain scale. The next e-gen revolution will be a bit of a marriage between these two.

*(L-R) **Mr. Ashish Garg**, Partner, BCG India, **Mr. Sharad Mohan**, Country Head – Retail Banking, Citi India, **Mr. Rajiv Sabharwal**, Executive Director, ICICI Bank, **Mr. AjitRath**, Executive Director, Andhra Bank, **Mr. Rajiv Anand**, Executive Director, Axis Bank, **Mr. Nishant Singh**, Founder and CEO, CRMNEXT , **Mr. Arindam Mukherjee**, Operations Director – Enterprise Business, Cisco India and SAARC.*

Session on 'New ways of leveraging technology and ecosystems for changing business growth'

Session moderated by **Mr Ashish Garg**, Partner, The Boston Consulting Group, India.

Panellists

- **Mr Ajit Rath**, Executive Director, Andhra Bank.
- **Mr Rajiv Sabharwal**, Executive Director, ICICI Bank.
- **Mr Sharad Mohan**, Country Head – Retail Banking, Citi India.
- **Mr Rajiv Anand**, Executive Director, Axis Bank.
- **Mr Nishant Singh**, Founder and CEO, CRMNEXT.
- **Mr Arindam Mukherjee**, Operations Director – Enterprise Business, Cisco India and SAARC.

Overview by Mr Ashish Garg

Since the theme is broad based with many elements to it, Mr Garg decided to cover a few of them in this session. He identified six relevant themes for the discussion:

- How banks can keep pace with the expected surge in payments.
- The opportunities and challenges posed by digital lending.
- Are fintechs and ecosystems a fad or are they the future?
- How banks are mining their data gold mine within and outside the bank.

- What we do not know about cyber security and technology.
- How banks can respond to the new functionality demands and develop maturity on organisation and processes.

A recent research study suggested that digital payments are growing phenomenally. It is expected that by 2020 a volume having the value of $ 500 billion will flow through digital payments. And half of these payments will be less than ₹ 100/=. Many bankers are already experimenting and seeing very good success with small ticket sized payments. By 2023, 50% of consumer payment transactions will be non-cash; and 50% of Internet users will use digital payments, up from the current estimation of 17%.

The traditional banks follow a 'bundled-up' model, with all products under one roof. Can payment banks disrupt this model by bringing the best of the breed to the consumer? Can they also manage liabilities, investment products, insurance and mutual funds, or tie up with NBFCs for borrowings?

UPI is creating a completely interoperable, brand new architecture. It is round the corner; hopefully it will be a game changer.

As regards digital lending, Mr Garg wondered where it can help the present challenges. Citing the example of rural banking, he pointed out that banks don't have proper products customised to farmers' needs. It seems like a vicious cycle. The ticket sizes are small, and there is high reliance on documentation. Manual, cash-based recovery is very high. NPAs in this sector are also very high, sometimes as high as 50%, resulting in very poor growth in rural lending.

However, a lot of new value chains have been emerging. Are these value chains useful in digital lending in certain segments, he wanted to know from the panel. He also questioned how banks that were able to get useful data would fare different from those that weren't.

Fintechs are emerging into various spaces such as capital markets, corporates or SMEs, retail, wealth and asset management. They are operating in technology clusters, either blockchain or data and analytics, or trading and investments. Funding in fintechs is at an all time high and it is growing exponentially. In 2015, $ 30 billion of VC money went into fintechs across the world. Many of these fintechs were still operating out of garages. Globally, banks too are participating in the fintech space. There are banks that acquire or set up PE funds to figure out where a promising fintech comes up and they acquire that and get their technologies on board. A lot of banks are happy to partner with fintechs and approach the market jointly. There has been a surge in fintechs in India too. He wanted to know how the eminent panel members saw this space emerging.

Coming to cyber security and technology, Mr Garg pointed out that in 2015, the known risks on IT and cyber security cost banks $ 50 billion. He observed that as banks start becoming more connected, the risks of hackers getting into the system, increasing limits for prepaid cards, or using DDOS attacks to make ransom demands, are also increasing. He wanted to know whether Indian banks report and understand true losses on account of cyber and IT risks, and which new technologies are relevant for banking to move faster.

Clearly, banks are gearing up to the challenge and the opportunities. BCG's research shows that they will require nine new digital competencies in the new ecosystem: big data and analytics; agile process experts; developing digital content; infrastructure groups; mobile interfaces; digital customer experience; risk and security; payments; and digital branding and marketing. He wondered how the banks were thinking about their new organisational capabilities to accommodate that.

Panellists' Views

Mr Rajiv Anand

Payments are core to the banking franchise, be they P2P, P2merchant, or Government payments. Customers may take a housing loan once or twice in their lifetime and a car loan perhaps about seven times in their lifetime. But they use the banks' debit and credit cards, ATMs, Internet and mobile apps on a daily basis. Therefore banks are very passionate about wanting to make payments as frictionless and ubiquitous as possible. Most banks are already offering these facilities to customers for free. The view is that they will drive engagement through payments and earn on fee and float with their other offerings such as mutual funds and insurance.

But the payment bank business model still needs to evolve. They cannot lend money; therefore, the traditional banks' ability to lend to customers through a payment bank could be one area of collaboration. There will be many areas of competition, but lending and fixed deposits are possible areas of collaboration. Since most transactions are free to the customer, payment banks will have to compete against these free services. They may be willing to pay money to acquire customers — but somebody has to pay for the transaction; it will be either the customer or the merchant.

The biggest contribution of fintechs to banks has been a fundamental change in the way the latter think about the customer. This also holds true for entities like Uber and Amazon. They are able to deliver intuitive customer experience. "Instant gratification has certainly helped us change the way we think," he remarked, saying that if we can get a cab in five minutes, we should be able to transfer money or get a loan instantly.

This would probably not have happened without the technology stack. "Various fintechs are chipping away at small problems," he said, and banks are happy to partner with them to be able to solve some of these issues. Thus even the incumbent banks have moved a long way in being able to stay relevant to the customer. Mr Anand disclosed that his own bank has just set up its accelerator called Thought Factory in Bengaluru, where they are working with start-ups. They are ready to partner with anybody, not necessarily only fintechs.

Some customers need to be encouraged before they get converted to digital. Mr Anand cited the example of one of their branch heads in a village. He merely demonstrated to the people how easy it was to be able to recharge their DTH, without mentioning mobile banking. Everybody in the village realised how simple it was to use, and he then explained that they need no longer travel to the branch to do simple transactions. The bank manager "needs to find a hook" to educate the customer and show them how simple the process is. "Once they get in, the adoption is pretty good," said Mr Anand.

"We live and die by data and everything we do is around data," he replied, when asked about his experience on how to use data effectively. The entire functioning of the retail bank is based on data. But cyber crime is something that banks will always have to guard against. It is an uncomfortable situation that most banks have to face and deal with on a regular basis. He expressed doubt about the acceptance of biometric authentication among the general public. "That is why maybe I am not a science fiction writer," he commented, in lighter vein.

The core of Axis Bank's retail lending business continues to be traditional loans against homes, auto loans and personal loans. Mr Anand disclosed that they are experimenting in the space of cash flow based lending, on the basis of data. For example, 'Nano Credit' has been launched for the really low income group. They have been able to use data from mobile phones and Aadhar cards, since this segment uses remittance facilities and pays utility bills. Using this data, they can assess income levels and are able to offer term loans from between Rs 7,500 to Rs 15,000. "It is a test and learn process both for us as well as the customer because this is the first time that the customer is actually borrowing within this space." This is how technology has helped banks manage operational risk and customer experience in the microfinance area.

Mr Ajit Rath

Mr Rath agreed with Mr Rajiv Anand that payments are core to the banks. But certain kinds of technology interventions have come into the system, and banks need to catch up. Fintech companies quickly come into the market and deploy them. Then again, they depend on the banks for distribution or collection because customers anyway maintain an account, and the collection account for mobile wallets has to be with a bank. Therefore, the entire payment of those transactions will travel through the banks.

He was asked whether, as payments become commodity, there would be challenges to the fee income of banks from transaction products and payment products. He observed that if Indian telecom companies were to be considered, they have probably the least revenue per user globally; yet they do good business because of the volumes. In India, small ticket size transactions have to be there, because their volumes can be quite large. The focus should be on handling this volume. There need be no worry about those transactions being less competitive in terms of pricing. The margins will come from the volumes.

A lot of exciting things are happening in the payment system with an entire ecosystem built up around PCI, Aadhar, etc. Fintech has opened up a whole lot of opportunities for banks to build products and get to the market very fast. One of the challenges that banks face is in selecting these fintechs. Historically, banks select people or technology partners through a tendering process where they are evaluated on their experience and balance sheets; suddenly this system has to change. Banks have to re-evaluate how to select the right fintech partner for technical development.

Big data is another area where fintechs are giving banks lots of hope. Fintech companies are very successful in working with banks in the business analytics area. If a fintech company can create a scorecard for a particular individual or SME based on external transactions, such a tie-up makes sense.

Mr Rath was then asked for his views on basic customer contact information that seems difficult to obtain despite banks having so much data. He pointed out that as banks migrate from branch banking to core banking, the customer who earlier was a branch customer now becomes a bank customer. But he agreed that even at this stage, banks still carry the baggage of old data having to be cleaned and migrated into core banking. "That is work in progress because of the large number of records," he felt. Online validation tools like UCIC and Aadhar will simplify the process. CRM will play a big role, but it should be phased out, starting with operational management.

Public sector banks face their own challenges, agreed Mr Rath. Often, their loyal customers are quite senior and not very conversant with technology. The newer, younger customers also need to be educated because people are not very careful when it comes to doing transactions on digital platforms. Within the organisation itself, there has to be continuous persuasion with the employees, and the learning management system has to be integrated with the HR function. His bank has an innovation desk which receives feedback from customers as well as employees about the new technologies, he revealed.

Mr Sharad Mohan

Mr Mohan was asked about his views on the future of digital play in acquisition and servicing.

"Digital acquisition and servicing will play a significant and very defining role in the future vis-à-vis the physical footprint," he said. Until now, acquisition meant filling a form and getting a banker's representative to meet a prospect. Over a period of time, this moved to the electronic channels in quite a significant manner. The paper form evolved to a digital form; and the face-to-face meeting started evolving to a telecon or a digital meeting. But the person still had to be present at a particular place and had to have a computer to be able to connect with the bank representative. That was still restrictive. The biggest change that has happened is the enabling of the acquisition process by the smart phone. With over 300 million smart phones in the country, and their rampant increase on almost a daily basis, the mechanism for banks and financial institutions to reach out to clients has increased manifold. Added to this, documentation is becoming simpler with Aadhar and e-KYC. Instead of people having to carry copies of their KYC documents physically, they can validate themselves through biometrics and e-KYC. An account can actually be opened remotely through a smart phone and through e-KYC and Aadhar.

Servicing is about the simplicity of conducting transactions through a multiple set of access channels. This is already happening in certain segments and will accelerate further as the digital process becomes simpler and is increasingly adopted.

The regulator is playing an important and supportive role in bringing all this to the fore. Relevant offerings by banks and financial institutions across a range of products will mostly be digital.

He informed the gathering that Citibank has its own fintech, operating in the US, called Citi Fintech. The idea behind Citi Fintech was to create an organisation which would cater to the bank's needs for technology development. "Classically, the bank has always adopted a long gestation period release methodology," he said. The number of releases coming out in the year is restricted by economies of scale and stability. But since "mobile is the way for the future," the bank's management decided to change the way it did business and worked on developing technology.

That was the reason why Citi Fintech was formed, with a very start-up culture. It is focused on the US market. In India or other regional markets, they have adopted the 'Citi Mobile Challenge' where they throw open a challenge to all of the companies that are operating in the banking technology area and are primarily using mobile to deliver that technology. In India, the 'Citi Mobile Challenge' was held during the previous October. Almost 1900 companies participated. They have now identified a set of companies and are working with them. "Fintech is somewhat becoming our way of life as we work with this rapidly changing world."

With solutions coming up "at the pace of light," there are now more solutions than potential problems. The ultimate beneficiary is the client. There is so much 'solution' available that it allows different banks to pick solutions specifically to meet their respective client needs. This is actually making the entire system quite frictionless.

Since conventional methods of finding solutions to problems are not going to be very effective, Citibank has initiated an 'Innovation Council'. Now everyone is involved in innovation; it is no longer reserved for a particular department. One of the reasons why some of these processes don't succeed is inertia, felt Mr Mohan. If the organisation develops a mindset to adopt digital interfaces with innovation as a driver, people will be open to anything new. Many of the current technologies are self-learning and cannot be taught. They are intuitively understood by young people. And if the employees adopt, then clients will also adopt. Citibank has one of the highest levels of digital adoption by clients. They achieved this by changing their conventional method of showcasing very digitally savvy people. They show normal, regular people trying to adopt to digital banking and taking charge.

He also felt that it is possible that in two years' time banks in India will be able to issue loans on mobile phones in less than five minutes. This is because they will have the ability to pull out the data for a new prospect fairly quickly. If the data can be accessed in real time, the bank can actually give instant credit to that client. His view was that this is not very far off in the future. It is actually happening to some extent.

Mr Rajiv Sabharwal

Using digital channels is gaining momentum by leaps and bounds. In the beginning, most of these channels were used for non-financial transactions such as viewing bank statements or ordering cheque books. The next wave brought financial transactions into play. Today, digital channels can be used to carry out virtually any transaction that happens at a bank branch. In Mr Sabharwal's opinion, the next wave will be on acquisitions and how these channels will become the engines for acquisition. Every customer should be digitally active and the bank should find ways of ensuring that they are made aware of these channels.

There are certain types of entities in the digital world who have the ability to attract many customers. Mr Sabharwal appreciated the amount of innovation that fintechs have brought into the system. Banks must look at such entities and decide about tie-ups with them. Tie-ups can reduce the cost of acquiring customers, which currently is the biggest challenge that banks face. The future lies in partnerships where both entities think of each other. Speaking about his bank's ethos, he said, "For us, a partnership has to be a lifelong partnership."

He informed that his bank segments customers by their usage of a combination of channels. If they are not active on one channel, they know on which other channel they can be approached. They have rolled out a multi-channel strategy whereby they have a single view of the customer across all channels. "Finding ways and means of integrating a customer across channels is extremely important," he said.

The evolution of the fintech space has brought about a shift in the way customer acquisition is happening. "Today there are entities which don't hesitate in throwing money to acquire customers," Mr Sabharwal observed. That is a threat to the whole system and does not augur well for a sustainable business model; something will have to be done to create a long-term, sustainable model. Banks will win in the long run because of their ability to offer comprehensive services. In the long run, people will demand comprehensive services coming from one service provider.

The quality of data is extremely important. It is important to work hard in the initial stages so that things become easier later on. It has to be enriched regularly. Big data can reveal information which is lying within the bank, and also what is happening outside it. Much of this was not available in the past but is available today, and is extremely useful. Today, a person who does not know technology, whether at the front end or in the back office, does not have a future. "There is so much of change happening in this space that the only way is to self-learn," he suggested.

He also felt that where banks will win in the long run is in their ability to offer comprehensive services. The reason for this is, in his opinion, because in the long run customers will want comprehensive services coming from one service provider. "Even in this social world, when you have to be on Facebook and Twitter and WhatsApp, who wants to open each of the apps. If somebody gives me one app through which I can access all of them, then life will be easier," he said, capturing the sentiment of the public in general.

Mr Arindam Mukherjee

There is plenty of user data from multiple sources. Coupled with that, the new innovation ecosystem, the cost of smart phones with data bundles, and most important, the regulatory activism around multiple payment banks is making the digital ecosystem very rife for people to come in and disrupt.

Cisco is working with multiple state governments in building the 'golden mile' for the smart city projects. A lot of entrepreneurship is happening in Andhra Pradesh, Rajasthan and Madhya Pradesh. Banks have potent ways to go in and cater to that. Those entrepreneurs will be selling their products on online portals. Their data is available online. It is not necessary to go through the traditional ways of verifying their credit credentials. Banks must get into the habit of 'smart partnering' by capturing those kinds of allied industries that are on the periphery of the business space.

Mr Mukherjee predicted that one profound change which is likely to happen in India will be in the data privacy architecture. When those architectures are ready, few of the large banks will tremendously increase the pace of innovation on this front. But it will be an alternate platform where fintechs will take the data feed and will massively scale out architecture; many smaller and emerging banks will supply the products. Fintechs will take those products and distribute them.

He also touched on the subject of cyber security. Citing the example of the 2014 J P Morgan heist, he recalled that the data of 76 million credit cards was breached in 48 hours. The fraudster did not really steal any data. One employee of the company left the two factor authentication window open for 48 hours. After this time, the windows got closed but the hackers left all of their tools and siphoned off all the data. They then placed a call asking for ransom. "If you really look at it, this is in the realm of trust and ethics of the people," he commented. Even with the most sophisticated technology, it happens. Today, threats are written with a zero-day attack. There is no way any IPS or firewall can stop that. The classic way to protect against these kinds of threat is to build a machine-learning engine that is augmented by itself; which goes back to the cyber threat centre and tries to polarise the threats across the network as they are proliferating. Banks are now waking up to these possibilities and trying to do their bit, but this has to be discussed at the boardroom level in terms of budgets and priority.

Mr Nishant Singh

Indian banks were always low income in terms of the fee they charged as compared to their global counterparts. Most of the fintech revolution that happened around the world was charged to fixed income. It was regressive to work with lot of banks outside India. One of the great things about India is that there is a lot of entrepreneurship in the way private banks have been run so far. India has the best digital infrastructure in the world. Indian banks are thinking hard and reinventing better than many of the global companies.

Before technology was available, there was a certain way of working. How does that way of working change with technology? Top management in any bank knows what needs to be done. They believe in it and push through those difficult changes which are enterprise-wide and not departmental initiatives. The question is how they do it. That is what makes the difference. The issue is centred on work design. For example, almost every bank has a CRM. But if they are still adding people to their operations team, it means something in the design didn't work.

There will soon be a segment of customers who are creditworthy and have a certain set of prerequisites. Their wait time will go down to zero. More and more customers want instant gratification. There are now some new platforms where the deposits that traditionally used to stay with banks can be deployed to a peer corporate which is looking for funds. Mr Singh sees this revolution as a work design problem where banks just have to go back and rethink how they have to do this in the new age.

*(L-R) **Mr. Bharat Poddar**, Partner and Director, BCG India, **Mr. Rakesh Singh**, Chief Executive Officer, Aditya Birla Finance Ltd., **Ms Usha Ananthasubramanian**, MD and CEO, Punjab National Bank, **Mr. Sanjay Bhatia**, Managing Director, Hindustan Tin Works and President, FICCI-CMSME, **Mr. Rajat Verma**, MD and Head - Corporate Banking, Commercial Banking, HSBC India.*

Session on 'Voice of Corporate and SME Banking Customers'

Session moderated by **Mr Bharat Poddar**, Partner and Director, The Boston Consulting Group, India.

Panellists

- **Ms Usha Ananthasubramanian**, MD and CEO, Punjab National Bank.
- **Mr Rakesh Singh**, Chief Executive Officer, Aditya Birla Finance Ltd.
- **Mr Sanjay Bhatia**, Managing Director, Hindustan Tin Works and President, FICCI-CMSME.
- **Mr Rajat Verma**, MD and Head - Corporate Banking, Commercial Banking, HSBC India.

Overview by **Mr Bharat Poddar**

Mr Poddar presented the results of a survey conducted by The Boston Consulting Group in 2013 and repeated again in 2016. The survey was conducted amongst corporates of various sizes,

to assess the trends in their behaviour. He shared some initial insights from the survey.

“How much share of its total banking business does a primary bank get from a corporate?" he asked. The majority of participants felt it was between 40% and 60%. But the answer, he disclosed, is 60% to 80%. The top two banks have the majority of the banking business of a corporate. The primary bank has almost 2.5 to 4 times the market share of a corporate. This is significant. If a bank wants to garner a higher share of wallet of that corporate, it is important for it to be their primary bank.

Over the last three years, corporates and SMEs are consolidating towards a two-bank model. There is greater consolidation happening between the primary and secondary bank. There are two clear trends: (i) the foreign banks have lost a lot of primary banking relationships; and (ii) the nationalised banks have lost significant primary banking relationships especially in the large and mid-sized companies. The private sector banks have grown this share of the primary banking relationship.

"What defines a primary banking relationship?" It is basically the current account and to some extent, working capital, cash management and the payroll, revealed Mr Poddar. Transaction banking products as a whole, and not mere lending, define a primary bank for the corporate or SME customer. That is a big insight into the behaviour of corporates, he felt.

He explained what happens if a bank merely lends to the corporates. Fifty nine per cent of the corporates surveyed take term loans from banks. Out of those, only 44 percentage points use the current account with the same bank from which they take a term loan. This means that "term loan providers are giving their balance sheets to the SMEs and the corporates, lending the money, but not really taking their fair share of these other transaction banking businesses." Other banks get this share of the business.

Large and small corporates were asked how happy they are with the banks. By far, the large corporates were most satisfied with the banking services across products. Especially on issues around service charges and price, there is a huge difference in the quality of the RMs that SMEs get compared to the large corporates. There was a significant drop in the quality of RMs across the span of the two surveys. But if a corporate is happy with a bank, will they do more business with that bank? Across products, the share of wallet of happier corporates with their primary banks is much higher. The corporates and the SMEs who are satisfied with the relationship with their primary bank give 15% more business to that bank. What are the issues about which they are not satisfied? It is mostly things like exception handling, service charges, technology, turnaround time and innovation. They are usually happy about products, price, flexibility and brand.

Sixty per cent of the corporates and SMEs surveyed said that while they considered pricing to be important, they would not switch their primary bank if the pricing were to change. If the banks do get their pricing right, they get 13% more share of business from satisfied corporates. But regardless of what RMs report, it is issues like speed and value added services that customers feel are important. Seventy per cent of corporates, and a much higher number of SMEs, would actually like their banks to offer services beyond banking, such as business support tools; help with accounting packages; simple benchmarking of their performance versus their peers; financial analysis of their cash flows; and expert guidance. Almost 40% of the corporates are willing to pay for these services because they trust their bankers and value these services.

The survey sought to ascertain if corporates and SMEs were aware of the digital offerings of banks. The results indicated that it depends on the type of offering. There is high awareness about checking of balances, updating account parameters and tracking bulk payments. Awareness is generally high about the digital availability of everything connected with payments, collections and transactions, and customers are generally satisfied. There is a medium level of awareness about trade and forex-related digital offerings. Those who use these offerings are satisfied with them. There is low or no awareness about investment-related transactions, vendor finance and dealer finance. The reason for companies not using these digital services is that they were not shown how to do it by the RM. "So the message for the banks is that if you invest enough behind educating the customer and hand-hold them to start using the digital properties, they actually get hooked to it and they are reasonably satisfied with these products."

The survey predicted that over the next five or so years, the activities with the RMs will continue to reduce. Seventy five per cent of the activities will become digital; mobile will certainly be used, but the desktop or laptop will continue to remain the main avenue for the corporates and the SMEs.

Panellists' Views

Ms Usha Ananthasubramanian

Corporates and SMEs are positively inclined towards the nationalised banks, but at the same time, the banks are losing their share. In the last year and a half or so, there has been a slowdown, with very weak pickup and no new projects. With all the big, mega and senior level projects that have happened in the country, it has been the contribution of the public sector banks in great measure that has brought investments in the country to this level. But there have been lack of demand, disrupted cash flows and irregularity of servicing.

"The world of financial services is changing rapidly," observed Ms Ananthasubramanian.

There are other attractive avenues that provide alternative funding mechanisms, like bonds and overseas borrowing. With these avenues, there is bound to be a shift. But public sector banks will remain a key source of funding for any of the projects that have to come in the country.

Banks have a problem in terms of their earnings. They are getting very conscious about capital conservation; they would like to have more AAA rated customers, so that they can manage their capital adequacy better. But AAA customers feel that because they are the best-in-class, they need not pay the bank anything more. Those who have migrated to the C, C1, C+ or D categories feel that they are so weak that banks should not expect them to pay even though the risk on them is very high. The B category customers, who are mid-corporates and medium account holders, get sandwiched in the process; it is from them that banks expect their earnings.

Timely delivery of credit is very important for small corporates and MSME entrepreneurs. The turnaround time must be cut short in such a way that they are not starved of funds, and at the same time there is timeliness in how the banks operate. They are excellent technocrats but they lack the financial acumen. Bankers need to hand-hold them in preparing their cash flows, and even their projects. Ms Anantha Subramanian called upon banks to work towards the all-round growth of entrepreneurs, complete with financing, provision of services, value-added propositions and digitalisation. "I think we will be able to see good days for the MSMEs," she felt. Speaking about Punjab National Bank, she disclosed that they have almost 21% of their books in MSME advances, with 285 dedicated branches for SME funding. They are in the process of unleashing a cadre of officers called Financial Counsellors, who will work with and guide SMEs.

Discussing the specific things that banks can do to improve customer satisfaction, Ms Ananthasubramanian felt that banks must be present through the lifecycle of the customer. They should not be there just to give a loan and then "watch what happens." It starts off as a very small relationship, but doesn't stop there. It progresses through the lifecycle, giving it many more products that matter to the individual entrepreneur or the staff or the working unit.

Segmentation becomes even more important. There is a category of women entrepreneurs coming up very fast; they cannot be ignored. Special products need to be developed for them because they are not into hard, industrial activities; they are into sophisticated and meaningful activities. Products for them need to be designed differently. Similarly, another upcoming segment is the youth segment. Clusters are groups where similar kinds of activities happen. It becomes easier for banks to step in, talk finance with the group in a manner that they understand, and then cater to their needs. Banks will need to leverage these areas in specific, specialised ways that will glue both the bank and the entrepreneur in a better way.

The role of the relationship manager cannot be undermined. He is the first connect and the entrepreneur depends on him for loans and other services, and also trusts him. The ride towards digital offerings has been very smooth. The role of the relationship manager will change as he shifts to the digital platform. Customer education becomes very important. Banks may invest in any number of products and services, but if they don't reach the customer, they remain as "mannequins in a showroom." Customer education can happen through the relationship manager. "Today, we have almost reached the finality," she said, alluding to the mobile revolution. "There is nothing beyond that." She felt that all new innovations will be in the small space of the mobile phone, and no bank can afford to lag behind.

Mr Rajat Verma

Mr Verma was asked how foreign banks looked at transaction banking, because traditionally they focused a lot on products such as current accounts, cash management and trade. His opinion was that besides products such as current accounts, transaction banking is also fundamental to the principle of lending. This is increasingly becoming true of all banks. All banks are using technology to converge towards common platforms; because of the initiatives taken in this country, and indeed over the world, the system towards which banks are converging is not very different between foreign banks, public sector and private sector banks. Transaction banking should therefore become much more interoperable in the future than it is today.

Regarding customer satisfaction, Mr Verma said, "For bankers like myself, it is really important to sometimes go back to school and listen." He felt that surveys could achieve that. They provide a means for banks to listen to somebody else talking about themselves as well as the industry. The concept is followed to a different extent in different institutions. Independent surveys which are not bank-specific are a well-accepted norm that is followed globally. They go fairly deep into the qualitative aspects of client feedback. On the retail banking side there are mystery shopping surveys, but they rarely go into very specific measures. They are taken quite seriously in foreign banks, and he felt that more banks should adopt them.

He described the move to digital, paperless transactions as "quite a revolution." UPI can now make all banks come on a common platform where transactions can be done instantaneously 24/7. In some ways, India has been able to leapfrog some of the other platforms that other countries have had. "That move has been so dramatic that it takes your breath away," he said. Today there are 10 crore clients of e-commerce. That number will double by 2018. Smartphones and 4G are all enablers. He praised Payment Corporation and other banks for the outstanding work they are doing.

Mr Verma suspected that not even all bankers may be aware of the "extent of change that is likely to come over the next few years." The most important part of this revolution is that the advantage that foreign banks enjoyed earlier with technology actually goes away because they are now on a common platform. UPI brings a step change in the payment systems across the country and provides a level playing field. "It is really exciting and banks should spend a lot more time informing their customers about the changes," he suggested. He felt that much more information should be available to clients to be able to absorb this dramatic change. The importance of the RM will not diminish with these changes. The RM construct is fundamental to banking, and that has not changed for 150 years. The changes may actually give the RMs more time to do what they should be doing, rather than transaction processing.

Regarding SMEs, Mr Verma observed that the highest NPAs are in the large corporate space, and the lowest in the microfinance space, with the SMEs in between. In the SME portfolios of various banks, the highest yielding client is the most creditworthy. Even though foreign banks are not very large, the performance of their SME portfolios can be quite strong. He felt that SME is the driver for India and banks should look to help them, not just with credit but in all other forms that are possible.

Mr Sanjay Bhatia

The MSME and SME sectors play a very important role in the development of the country and need nurturing. They suffer severely due to high rates of interest; added to that, the lending process is paper-intensive and cumbersome. In particular, MSMEs find it hard to manage the process. There are many issues that they struggle with, yet they have no option but to depend on banks because they are always short of cash.

He suggested that repayment of term loans should be based on the cash flow of the particular project. Instead, banks have a schedule of three to five years for repayment. Banks are more wary of rescheduling repayments with MSMEs and SMEs compared to corporates, Mr Bhatia observed.

Commenting on what banks can do different, Mr Bhatia referred to the Nayak Committee Report that recommended that working capital should be 20% of the turnover, instead of asking the promoter to give a 25% margin. Perhaps banks could have specialised branches for this sector, since it needs special nurturing, like they have for industrial finance or exports. In addition, relationship managers should be specially trained to hand-hold the SME sector. They play a very critical role in the development of the sector. Funding for these enterprises should be available at the right time when they need it, to give them an opportunity to grow. That is the key for their survival. Mr Bhatia felt it would be good in case banks can design a flexible digital platform that can provide end-to-end services for SMEs and MSMEs, with a simple lending process. He cited a study which showed that there is scope to increase lending to the SME sector by Rs 60–70 thousand crore. That is good business waiting in the wings for banks. "After agriculture," he said, "if any sector can provide employment, it is this sector."

There is very low Internet and mobile banking penetration among the MSMEs. They would welcome it if digitalisation can be used to speed up the loan process and reduce the paperwork. Banks can actually leverage digital to improve the competitiveness of such enterprises. But he also expressed fear of misuse. "Cyber security is important to look at," he advocated.

Mr Rakesh Singh

SMEs are a big driver of any economy. In India, they contribute 14%–15% of the GDP, compared to 50% in China. They have to play a much larger role in the Indian economy. This is a segment which is underserved by the current banking structure. Large banks focus mainly on the large corporates or the consumer. "Somewhere, the SME falls between," Mr Singh regretted.

Today, almost 60% of SMEs don't have access to formal credit, and MSMEs are worse off. NBFCs can play a strong role to support them. They need customised solutions. In such a large and diverse country, connecting with the MSMEs can be quite a challenge. Technology must be leveraged to reach out to them. Mr Singh pointed out that this is a huge opportunity.

If banks or NBFCs can offer basic value-additions such as faster turnaround times, or money when it is required; and if such solutions can be customised based on needs rather than "just providing cookie cutter working capital limits," Mr Singh felt that SMEs will be able to churn their turnover much faster and grow their businesses. They are willing to pay for these value-added services. Pricing is just one parameter in their decision making. What really matters is whether the bank or the NBFC can match up with their growth expectation and understand the limits they are looking at with a timely offer of credit.

Digital usage is very low today. It is used mainly to check balances and payments. But things are changing fast, Mr Singh observed. The new technology, he predicted, will change the entire banking landscape. It is very important for bankers to make things simple from the customers' point of view. He gave an example: When an SME or an MSME applies for a business loan, the size of the loan file is extremely thick. Two thirds of that file is the bank statement of the undertaking over the last six months; some credit analyst then has to sit and study how many cheques have bounced, and what the banking turnover is. All this can now be done in minutes. The entire bank statement can be analysed immediately. These technologies are now available, and banks must collaborate with different service providers to bring them to their customers. That will be critical to turn around disbursement for SMEs and MSMEs.

"We are in very interesting times," declared Mr Singh. He predicted that banking and financial institutions will change drastically in the next three to five years. Payment banks have been given differentiated licenses; small bank licenses have been issued; NBFCs have grown; RBI is now offering on-tap licenses. Digital will play a big role. Once all this happens, the underserved segment of the Indian economy will be able to get credit. That is very promising. He called upon all financial institutions to work towards this goal. He expressed optimism in the way banks can serve the SME sector which is a very integral part of the Indian economy.

*(L-R) **Mr. Mohan Jayaraman**, MD, Experian Credit Information Company of India Pvt. Ltd. and Country Manager, Experian India, **Mr. Melwyn Rego**, MD and CEO, Bank of India, **Mr. P K Gupta**, Managing Director (Compliance and Risk), State Bank of India, **Mr. G Gopalakrishna**, Director, CAFRAL, **Mr. Abhishek Bhattacharya**, Co – Head, Banks and Financial Institutions, India Ratings and Research.*

Session on 'Capitalization challenges and new Basel norms for the new frontiers in risks'

Session moderated by **Mr P K Gupta**, Managing Director (Compliance and Risk), State Bank of India

Panellists

- **Mr Melwyn Rego**, MD and CEO, Bank of India.
- **Mr G Gopalakrishna**, Director, CAFRAL.
- **Mr Mohan Jayaraman**, MD, Experian Credit Information Company of India Pvt. Ltd. and Country Manager, Experian India.
- **Mr Abhishek Bhattacharya**, Co-head, Banks and Financial Institutions, India Ratings and Research.

Overview by **Mr P K Gupta**

Mr Gupta began by observing that more than risk, capitalisation is a much bigger challenge for banks in India, particularly the PSU banks. One of the main reasons for the challenges that banks face is the AQR. It has led to an increase in the NPA levels that banks declare and forced them to increase the provisioning that they make. As a result, their profitability ratios and other performance parameters have dropped drastically. This makes it even more difficult to raise capital from the market.

RBI has announced a timetable for the Basel implementation, with full implementation to take place by March 2019. The requirements go up every year. Some banks are barely able to manage their regulatory requirements. Mr Gupta was apprehensive about whether such banks would be able to meet the Basel norms by March 2019. He disclosed that most banks in India still follow the standardised approach, although a number of them have approached the RBI to move to more advanced approaches.

Even before Basel III can be implemented fully, there is talk about Basel IV. The BCBS realised that when Basel III was getting implemented and banks had a lot of discretion in using their internal models, there were huge differences in the RWAs used by various banks. The intention is to bring in uniformity through a more standardised approach. "The basic minimum floor should be the same which should be used by all the banks," Mr Gupta explained. Already, he said, implementation of Basel III is a huge challenge. Changing the scores midway will increase these challenges further. "I don't think we are, at this point of time, still fully ready for even the Basel III implementation."

There are two sources from which banks can raise their capital: from internal accruals and from the market. Internal accruals are the profits that they retain after the payment of dividend. With the AQR provisioning going up, most banks have been declaring losses rather than profits. This means that whatever capital they had is offset by the losses they are declaring. This in turn leaves them with no capital to do further business. Capital is needed for growth, and it is not available. In such circumstances, it is very difficult to go to the market and raise money. So it is a catch 22 situation.

PSU banks have an additional source from which they can raise capital, which is the Government. "The Government, being the largest owner, can always invest money." But, Mr Gupta added, there are limitations to how much the Government can invest. Last year, the Government announced capital infusion of Rs 70,000 crore over a four year period into the PSU banks. Some relief also came from some RBI relaxations regarding FCTR being used for the purpose of capital. In addition, they allowed real estate revaluation gains with a haircut of 55% to be used as capital.

Luckily, the results of a stress test recently released by the RBI showed that Indian banks were well-capitalised at the systemic level and should be able to meet their challenges. Another aspect of the Basel risk management process is the liquidity risk. Banks are required to maintain 70% of their liabilities maturing in the next 30 days as high quality liquid assets, called LCR. This value will progressively go up to 100% by 2019. At present banks are able to manage this because of some relaxations introduced by the RBI. Eleven per cent out of the twenty one per cent of SLR is now being used for LCR. Since the credit demand is low at present, the banks are able to manage their LCR. If the credit demand picks up, they may face a liquidity risk.

Growth in deposits has also not been impressive. After a period of many years, it has dropped to below 10%. That may also pose a challenge in managing liquidity. One way they could reduce their liquidity requirements is through non-callable deposits, but that has not taken off. The RBI has also relaxed the conditions for AT1 issuances. Provident funds have been allowed to invest in AT1, with a limit of 2% of their corpus. The big investors in the market, felt Mr Gupta, are the insurance companies. But so far the IRDA has not allowed them to invest. Other potential investors are the HNIs. But communicating the risk to them is difficult. "How can we develop a market where the people are willing to take a risk?" he asked. "Unless we are able to expand the investor base in India for AT1 instruments, I don't see much happening as far as that instrument is concerned."

Panellists' Views

Mr G Gopalakrishna

Indian banking definitely meets the minimum capital requirement under Basel III on an aggregate basis; but this comfortable position will become very illusionary once the credit demand picks up. India is a bank-intensive economy; bank lending is the major source of growth. Currently the bank credit to GDP ratio is very low, around 55%. Mr Gopalakrishna pointed out that this is one of the lowest ratios even among the developing countries. "If we want to grow in future, this ratio has to go up substantially," he declared. He emphasised that banks need capital, not because of Basel III, but for growth, particularly because of initiatives such as 'Make In India'. The demand for credit will grow substantially. Banks will therefore be required to raise capital.

Mr Gopalakrishna cited two data parameters that the banking system will need to meet the Basel III requirement by March 2019:

(i) The RBI had estimated the capital requirement for meeting Basel III at around ₹ 5 trillion. Out of this, ₹ 3.25 trillion would be in the form of equity capital and ₹ 1.75 trillion the CET. This was based on a 20% credit growth estimate by RBI.

(ii) The Government of India estimated the extra common equity of the public sector banks at around ₹ 1.8 trillion over the next four years. This was based on a 12%-15% credit growth estimate.

The Government also promised Rs 70,000 crore to meet the Basel III minimum requirements in the next four years. The public sector banks will have to raise the rest of the amount from the market, but it is becoming difficult to raise tier I and tier II bonds. If banks are not able to raise additional capital under tier I or tier II, that burden will also fall on the Government.

He explained why banks are facing this situation. There were some governance issues after 2012; many accounts, particularly infra and steel, started becoming NPAs. Banks went on the back foot, with hardly any credit growth. With almost no growth, there was no need for them to raise capital. Between 2012 and 2016, many corporate boards went to the market and issued ECBs, CPs or bonds. With the demand on the banking system reduced, banks became complacent and didn't raise capital beyond what the Government was to give them. Consequently, the market price of the public sector banks fell; today, many of them are quoted at one third of their book value. Under these circumstances, it is difficult for them to raise capital.

Then came the AQR process, and all banks were directed to reveal their NPAs and provide for them. Mr Gopalakrishna felt that presently the market is satisfied that "most of the cleaning has happened." He predicted more adjustments in the days to come, so that the current books of banks reflect the correct position. With this, banks will be able to convince the market that the current quality of their assets is completely reflected, and be able to improve their earnings and build some capital. But he cautioned that "the prospects for the public sector banks are going to be very difficult in the days to come."

He also spoke about the new frontiers of risks. He was dismayed that most Indian banks, especially public sector banks, do not have a clear risk management policy or a governance framework. "Unless we improve the risk governance and risk management system, things are going to be difficult in the days to come." This is especially because banks are now on the threshold of Basel IV. He offered some suggestions to the public sector banks, based on a survey on risk management: they need to strengthen their risk management departments with adequate staff; risk management should go much beyond being a mere compliance function; public sector banks should have an operating risk model in place; and they should have a buffer for their operations. He called for greater exchange of information among banks. There is now a lot of information available, as part of CRILIC. He advocated shared services for public sector banks.

Mr Gopalakrishna was asked whether, in his opinion, the RBI should be more relaxed in terms of capital requirements for banks in India. He said that although the RBI has not disclosed the rationale behind some of its actions, the most apparent reason is that the minimum requirement in India is 9% as against the Basel norm of 8%. Broadly speaking, the risk management system in India is low compared to that of the developed economies. Indian banks are not permitted netting of collateral. There are other issues where Indian norms are more stringent. For these reasons, till 2012, the overall compliance and the banking system was much stronger. Subsequently some of these conditions were relaxed.

He made it clear that he was in no way implying that banks in other countries are very efficient or well-capitalised. The difference is that European and US banking authorities have been doing a series of stress tests which are so stringent that many banks were sent back to the drawing board and returned with revised capital requirements. He suggested that India should also go in for stress testing analysis. That, in his opinion, will improve the banks' capital adequacy and our overall banking system.

The RBI has expressed willingness to allow an LCR of even over 11%, but on a graduated basis. If they raise the LCR drastically, the entire portfolio market will be at risk. Currently banks are comfortable with their liquidity position and the RBI is willing to relax the limit. He agreed with a participant's view that the RBI should reconsider its decision on the dividend policy for the public sector banks.

Mr Melwyn Rego

Mr Rego's discussion focussed on the travails that accompany the paucity of capital. In the past, banks were growing and generating internal accruals. "This plough back was generally adequate to take care of moderate growth," he said. But all this changed during the course of the year, with the recognition of weak assets, stressed assets, NPAs and AQRs.

The Basel III capital requirements are intended to ensure a more robust global banking system. The enhanced capital requirements are intended to provide a cushion for all possible losses that banks may incur. The challenges arise in operationalising and implementing the new Basel capital norms. As per the Basel III regulations, capital requirements, including the capital conservation buffer at 11.5% of risk weighted assets by March 2019, puts a lot of pressure on the banks. The CCB will be 2.5% by FY 2019. If RBI sees the credit to GDP ratio growing very rapidly, that would trigger off the countercyclical capital buffer and raise the requirement by another 2.5%. So in the normal course, the CRAR would need to be 11.5% by March 2019, and even higher if the countercyclical buffer is taken into account. For systemically important banks, this could go up by a further 1%–2%, putting enormous pressure on them to raise capital. Basel III norms have put a burden on the entire banking system.

Referring specifically to public sector banks, Mr Rego informed that the Government of India estimate for their capital requirements up to FY 2019 is Rs 1,80,000 crore, of which the Government will infuse Rs 70,000 crore. He agreed with some published studies that these estimates are on the lower side, because they were ascertained prior to what happened during the last year, when losses incurred by banks aggregated around Rs 15,000 crore. The July 2016 Fitch ratings estimated that Indian banks would require around USD 90 billion of capital to meet their Basel III requirements up to FY 2019. Eighty per cent of this amount will be required by public sector banks. Fifty per cent of the requirement will have to be met by core equity, and the balance by tier I debt capital instruments.

So on the one hand, capital needs have come down because of lack of growth; on the other, they have increased because of the stress in asset quality. India Ratings, in its August 2016 report, suggested that PSBs would require around ₹ 1.1 lakh crore as tier I capital, ₹ 40,000 crore as CET1 and ₹ 70,000 as AT1 bonds to achieve a bare minimum of 9% CAGR till FY 2019. This is over the ₹ 45,000 crore which needs to be infused by the Government of India in the remaining tranches. The quantum of fresh slippages may come down in FY 2017 and FY 2018, post AQR, the report indicated. Mr Rego agreed with the report, with the following caveat: what has not been taken into account with the NPAs that have been recognised and are on the books of the banks are the outstanding non-fund based limits. These can get translated into fund-based limits when the LCs devolve or when the BGs are invoked. In addition, banks who have sold their assets to ARCs will also have to take the hit when the SRs are revalued. The quantum of capital to be raised is quite large.

He then discussed the challenges in raising capital. Until 1994, 100% of the PSB capital was owned by the Government of India. With the amendment in the Nationalisation Act, PSBs started accessing the markets to raise equity. Today, public shareholding in PSBs is required to be at a minimum of 51%. Internal accruals will not be sufficient to meet these requirements on an ongoing basis. Hence banks will need to access the markets. The erstwhile focus was only on growth, with not too much attention being paid to raising of capital, which came primarily through plough back.

Presently, the main issue regarding equity sale by most PSBs is that their price to book is less than 0.5. Till such time as the clean-up happens, it will be challenging for them to raise capital; if the need becomes acute, they will have to raise the capital whatever be the price. This would be at the cost of dilution for the existing shareholders and will have repercussions on growth.

Speaking about retail growth, Mr Rego pointed out that it should be considered not only from the angle of risk mitigation, but also from that of capital conservation. Another avenue is the Additional Tier1 bonds. But the AT1 market is yet to develop in India due to lack of investor appetite and regulatory hurdles. The appetite for these bonds will remain quite meagre unless insurance and pension funds are allowed to invest in them. Thus far, no Indian bank has tapped the market for AT1 bonds.

On 1 March, the RBI came out with certain relaxations to what could constitute tier1 capital. While this has helped significantly in shoring up tier1 capital, "there is a need to differentiate the quality of capital." The profitability of a bank with a net worth of ₹ 20,000 crore will be quite different from one with ₹ 37,000 crore, he explained.

What matters finally is net interest income. "The general feeling is that the worst is over and that now we are on the upward trend." Mr Rego tended to agree with that view, provided banks factor in the ageing factor of their NPAs; if these assets do not recover or get upgraded into performing assets, the ageing factor will come into play, and the provisioning requirements will become quite significant.

RBI has permitted banks to issue tier1 and tier2 bonds to retail investors, provided the buyers fully understand the complexity and risk of such instruments. The attendant risk to retail investors is higher compared to that of other debt products. Tier2 bonds are relatively easy to sell and that has been done by most banks. SEBI has proposed new rules for AT1 bonds. The proposed norms for retail or public issuance of bonds issued by SEBI set the minimum investment at ₹ 2 lakh so that only well-informed investors enter this niche market. SEBI has also proposed characterisation of risks under the draft prospectus of AT1 bonds. The SEBI disclosure format for AT1 bonds is transparent enough to inform retail investors about the risks involved in clear and easy-to-understand language. Mr Rego suggested that banks and IBA should start investor programmes to inform retail investors about AT1 bonds.

Another way of raising capital is to identify non-core assets. Sale of these will help to augment capital. The growth strategy of banks will need to be driven by capital. Hence all banks will need to focus on capital conservation.

"I think the Reserve Bank of India has always been responsive to the needs of the banks," Mr Rego said. "When you look at the strength of the overall banking system I don't think anyone can question that." He was of the view that the LCR issue is not worrying too many banks, since the RBI has relaxed the SLR, which for these purposes can be treated up to 11%. He expressed confidence that when credit growth does pick up, the RBI will respond accordingly and make reasonable relaxations. He agreed that the current 21% of HTM is quite high; a larger portion of that could probably be used to meet the LCR requirements.

As per Basel norms, the leverage ratio is 3%. In India it is 4.5%. Most banks are able to meet that today, but that will also be a challenge in the days to come when credit growth picks up.

Mr Rego described the Deep-Discount Bond, a 25-year bond with an interest rate of 15.5%, which was issued for the first time in the early 1990s. A person investing ₹ 2,700 at that time stood to get ₹ 1,00,000 after 25 years. It appealed to the market. All efforts were made to educate retail investors. But when the call option was exercised after 10 years, there was a hue and cry. It was ahead of its time, Mr Rego explained. He feared that the same issue will crop up with AT1. There will be teething problems, but ultimately banks will have to go to the retail market to raise AT1 bonds after sufficient education. He advocated that they should be restricted to high net worth individuals with a minimum ticket size.

Mr Abhishek Bhattacharya

Mr Bhattacharya began by putting capital estimate analysis in perspective. So far, he said, growth estimates came from a top-down view. If GDP growth were at a nominal 12% to 12.5%, credit growth would have to be about 14% to 14.5%. But from a bottom-up view, things look different. From this angle, the growth that public sector banks are looking to achieve is the bare minimum required to absorb the pressure which could come from credit and operating costs. He predicted that there will be lot of pressure in terms of NPL ageing, which will keep the PnL subdued for at least the next 12 to 18 months. While some of the large public sector banks may still aspire for double-digit growth, most of the mid-sized public sector banks will barely manage single-digit growth. In fact, he said, some could even see shrinkage for a year or two.

Based on these assumptions, Mr Bhattacharya put blended CAGR at 9% for the next two to three years. This is the slowest growth over the last 20 years. The capital requirement according to these assumptions is about ₹ 1.0-1.1 trillion in tier1; that implies a 30% dilution from the current net worth base for most mid-sized banks. If the growth figure is deemed to be higher, every percentage point could mean an additional capital requirement of ₹ 350-400 billion for the system as a whole.

So what happens to growth, Mr Bhattacharya asked. When banks step into real economic recovery mode in one or two years' time, this will be a challenge. That is the time when banks will start feeling the pinch. The equity requirement may be about ₹ 400 billion. The requirement from hybrid instruments or AT1 bonds will be about ₹ 700 billion, he estimated. So far, banks have been able to raise about ₹ 170-180 billion through various sources. "We don't have the investors who have the appetite to pick these bonds," he noted, adding that insurance companies and pension funds have been hampered by regulatory hurdles.

Price discovery has also been an issue. Initially, in most of these bonds, there was a gap between the rating level and the pricing. Some of those challenges are now getting addressed, Mr Bhattacharya observed. There is more visibility in terms of the quality of earnings for banks, and the pricing is catching up. But, he pointed out, some intervention will be needed if regulatory hurdles come in the way. He advocated raising of more capital now rather than waiting for FY 2019 when a lot of crowding out could happen.

Post AQR, it was expected that about 20% of bank credit to corporates and SMEs would be deeply stressed. About half of that got recognition either as NPAs or standard restructured. AQR ensured transition from standard restructured to NPA, and these accounts got provided for. Some of them moved from 5% to even 45% or 50%. Still, about 6%-7% of them would fall through most filters of very low interest coverage, very high debt to EBITDA ratio and high debt to equity ratio, although they would be reflected as standard in bank books. Most of these are viable assets with a longer life. Mr Bhattacharya expected that slippages will start dropping, but there will still be pressure on PnL accounts as the NPAs start ageing. Hence, even in FY 2017, a lot of banks would be under pressure in terms of their physical recovery, "but going forward, we might be looking at the cusp of recovery." He also felt that banks would need more systems in place to manage liquidity when they move to a daily compliance regime.

He suggested stronger focus on AT1 and exploring ways to increase the investment appetite. So far, he said, the focus was on optimisation of capital, with a lot of dependency on the Government to provide succour as and when needed.

In AT1, the need is much more than the Government support in terms of capital. So while bailout capital is available, the triggers for any AT1 coupon deferrals are higher. Three things that need to be looked at are the risk of coupon deferral; the risk of a write-down; and the linkage of the bank with the unsupported credit profile. Once all the risks are spelled out transparently, banks will be in a much more comfortable position. The risk of coupon deferral in public sector banks was high during the year. Yet, in Q1, most banks that were in trouble still reported a little profit. He felt that the threat is less in the immediate future, but coupon deferral remains a risk. If the issuer demonstrates that he is able to call over a five-year period, that will instil confidence in investors.

The ideal situation would be to be in a position "where you can demand capital from the market at will." This would come with improved efficiencies, and increasing ROA and ROE. That was the desired situation that Mr Bhattacharya advocated.

Mr Mohan Jayaraman

Mr Jayaraman's focus was on retail banking, and the internal accruals benefits that banks could get as a consequence of putting better processes in place.

India was largely a corporate banking country till about 2000, when private sector banks began getting into retail banking in a big way. Around 2005, the public sector banks also entered the retail lending arena. That wave of retail lending as a growth instrument has continued to date. For most banks, the key strategy for growth revolves around retail, provided risk remains contained and capital requirements are reasonably well-known. But it is possible to use capital more optimally within the retail space, he said.

In Indian banking, about 35% of the loans that are underwritten come into the system from 'new to credit' profiles. These are people who do not have a credit profile within the banking system; banks spend time and effort on such loans. The remaining 65% are people who have a credit profile and some level of exposure in the banking system. This part of the audience can be underwritten better, using information that is already available.

But India still has a long way to go in using credit risk models fairly aggressively within the banking space. Most of the credit underwriting is done manually by credit underwriters who sit either in the branch or in a central office. The processes are policy-driven with no uniformity. There is little statistical control that banks can keep on the way the portfolio is underwritten. There is another method used by the western world and by any banking system that is used to giving retail loans. Retail credit can be evaluated through scoring, through statistically-driven mechanisms that can actually evaluate the risk and the economic capital on the underlying portfolio. The Indian banking system can move into this practice in a significant way. "Manual systems can complement these automated systems but they shouldn't be the mainstay as they are right now," said Mr Jayaraman.

Efficiency can also be brought into collections. Mr Jayaraman explained that at present in the country, one rupee spent in collection has about 30% of the efficiency of a rupee spent elsewhere in the world in the ability to recover money. A lot can be done in the retail space to put clear models in place that can evaluate the means by which collection strategies can be implemented, and improve efficiency. About 90% of the collection that happens in the country at present is still field-driven; a lot of this can be moved towards the non-invasive methods that most countries use. Some of these processes can add a lot of value to the banking system.

Implementing these techniques in risk evaluation and collections, "this growth that the banking system is making into the retail space can actually be kept well in control," Mr Jayaraman felt.

Speaking about leverage risks and the income estimation methodologies that banks need to put in with respect to portfolios, Mr Jayaraman felt that there is a means by which statistical modelling can bring in the base evaluation of all of these. Most of the 2007-08 subprime crisis that the Indian banking system went through was related to leverage risks that the banks took on, or the wrong products being sold to the wrong profile of customers; both of these can be remediated today with information that is available within the bureau system, and with models that can be built to better evaluate these risks.

Retail is a key part of the strategy for the banking system. "There is, however, an urgent, burning need for us to put a few building blocks in place that will help us build that portfolio optimally," said Mr Jayaraman.

*(L-R) **Mr. Prateek Roongta**, Partner, The Boston Consulting Group, **Mr. Abhay Gupte**, CEO, Manipal Technologies Ltd, **Ms Debopama Sen**, Head, Treasury and Trade Solutions, Citi India, **Mr. M K Jain**, MD and CEO, Indian Bank, **Mr. Rajeev Ahuja**, Head – Strategy, RBL Bank, **Mr. Asit Oberoi**, Group President and Global Head, Transaction Banking Group, Yes Bank, **Mr. Kiran Shetty**, CEO, SWIFT India.*

Session on 'Transaction Banking: New Frontiers with Digital and Technology'

Session moderated by **Mr Prateek Roongta**, Partner, The Boston Consulting Group, India.

Panellists

- **Mr M K Jain**, MD and CEO, Indian Bank.
- **Ms Debopama Sen**, Head, Treasury and Trade Solutions, Citi India.
- **Mr Rajeev Ahuja**, Head – Strategy, RBL Bank.
- **Mr Asit Oberoi**, Group President and Global Head, Transaction Banking Group, Yes Bank.
- **Mr Abhay Gupte**, CEO, Manipal Technologies Ltd.
- **Mr Kiran Shetty**, CEO, SWIFT India.

Overview by **Mr Prateek Roongta**

"Transaction banking in India is poised for a significant growth in the coming few years," began Mr Roongta. He explained that it provides a superior return on capital for banks, with its attractive profit margins and low capital absorption. However, as client requirements get more refined, there is a growing need for sophisticated products and nimble servicing. Banks and other players who are able to cater to these rising client needs will be better-positioned to manage transaction banking in the next few years.

He shared the findings from some recent corporate research done by his organisation. In a recent survey that they did with corporates around the world, the latter were asked for what banking needs they were using digital the most. Eighty five per cent of the companies polled responded that they were using digital for their transaction banking requirements like payments, cash management and trade finance. A deeper drill-down into what is driving digital revealed that the thrust for digital comes both from customers as well as from banks. Customers are looking for convenient, flexible and timely solutions. They want platforms and channels to connect with and interact with other business users. "They are not happy with standard out-of-the-box products; they want tailored products, and tailored ways to interact with their bank."

Digital is changing the business approach across all dimensions of banking. Relationship models are moving from being RM-focused to self-service. Transaction channels are evolving from branches as fulcrums to anywhere-anytime banking through online channels. "One-size-fits-all does not work anymore," said Mr Roongta. "Clients are looking for customised products and value-added services using digital." He added that the risk appetite of banks is also changing. Banks now do not just look at the traditional way of evaluating risk, but look at big data-based or analytics-based risk ratings. Pricing is changing too; the 'rack rate' price is no longer relevant. Banks now use dynamic, portfolio-based, customised pricing based on the data that they have about every client. Banks no longer have to deal with incomplete client data. Today, with technology, they have an end-to-end, integrated view of their clients. They are therefore able to offer their products in a more relevant and appropriate context.

He cited examples from around the world. Wells Fargo, a transaction banking champion, launched an online portal which is a commercial electronic office that offers more than 80 products of the bank to its customers online. Barclays offers banking products and value-added services to its commercial and mid-corporate clients through its 'My Business Works' portal; just offering these products improved the satisfaction rate of Barclays' customers by 80%. Standard Chartered has a mobile app called 'Straight2Bank' which allows the CEOs and CFOs of their corporate clients to authorise transactions using their mobile phones.

"What has been most remarkable over the last few years," continued Mr Roongta, "is the entry of non-banks, fintech companies in the space of banking, and more specifically transaction banking." Hundreds of new age start-ups have entered this arena and offer very niche technology oriented solutions, a large number of which are in the transaction banking and payment space. Companies like Square and Intuit use technology to enable small businesses to accept digital or online payments. For large corporates, companies like Ariba and SAP enable host to host integration between the bank and the ERP platform of these companies. These non-banking companies are providing solutions which make banking easier. Almost two thirds of all payment transactions done by companies around the world last year were digital. "Digitalisation has gone up in India as well, but it lacks the pace that we have seen around the world," said Mr Roongta.

As part of the study, corporate clients in India were asked to rate their banks on their strengths and weaknesses. They were very happy with their branch networks and the quality of the RMs. But they were unanimously unhappy with the innovation and technology provided by banks in India. One of the main pain points of companies was that banks do not provide end-to-end solutions. For example, forex and trade finance offerings of banks are not integrated; clients are asked to submit the same documents several times for a single underlying transaction. In addition, clients feel that banks only sell products and do not offer solutions; they would like banks to understand their problems, and offer relevant solutions. Corporate clients are ready to embrace digital. They don't want to go to a branch if they can get the right solutions and user-friendly interfaces that make banking convenient rather than cumbersome.

Almost three quarters of the companies surveyed are able to check their balances or change signatories in their accounts online. When it comes to trade, forex and investment transactions, a quarter of the companies polled are not even aware that they can do it online. Another 50% are aware but still do not use these channels. A mere 20%–30% use these channels to do such transactions online. "Banks will need to do a lot more in building awareness about their digital offerings and encourage corporates to use these digital offerings," Mr Roongta suggested.

The hesitation of companies to use digital is mainly for security reasons. One out of every five companies polled cited security as a big barrier to their using online channels. The other reasons are ease of use, and ease of linkage with the accounting software of the corporate and the banking systems.

In Mr Roongta's view, the following five aspects are important for banks to build a best-in-class integrated digital platform:

- Provide integrated access and intuitive experience through easy-to-use, easy-to-understand digital channels.
- Provide seamless on-boarding across products.
- The digital products offered should be relevant, circumstantial and data-driven.
- Empower customers through customisation. The days when one-size-fits-all, out-of-the-box products can be sold to all clients are over.
- Cater to end-to-end needs of the customer. Client requirements are becoming complex. An end-to-end, technology-enabled digital experience by the customer will go a long way in driving the adoption of digital channels.

Panellists' Views

Mr M K Jain

Most corporates are becoming global, in Mr Jain's view, because their business becomes global. Many corporates have become MNCs with overseas business partners; hence they have to embrace the technology. Banking itself is becoming very complex with new derivatives and initiatives entering the scene. The delivery time has shortened. "Only technology can provide these services," he said.

There are two aspects regarding the preparedness of corporate clients to adopt technology: transaction banking, and non-transaction banking. Most corporate clients are very well-positioned as far as transaction banking is concerned. They are demanding a lot of technology products and are ready for end-to-end solutions in their supply chain management.

This is what banks must offer transaction banking; there is no way out. The challenge, Mr Jain said, comes from non-transaction banking, mainly credit approvals. For this, the back office must be ready and adaptable. Corporate clients need to have the exception approval process in place. That is work-in-progress. They also look for cost reduction. In fact, he said, the increased competition among banks is not for growth; it is for the wallet share, and for that, value-added services must be provided.

He cited two examples of what Indian Bank offers to its corporate clients.

- A corporate client was facing reconciliation issues with its current bank. Indian Bank offered a technology product that made reconciliation seamless.
- A big government client had around 51,000 dealers across the state. Taking orders from them was extremely cumbersome. "We provided our solution by connecting their server with our server in one minute, and we were able to open around 51,000 virtual accounts of all the dealers."

Mr Jain also touched on financial inclusion. He said there were three aspects to it

- Basic banking: Presently, he said, around 1.90 lakh AEPs and RuPay card-enabled machines are available, but their availability is bank-specific, not sector-specific. Interoperability is an issue that needs to be addressed. Banks are handling around three crore PMJDY accounts per month. They need to scale up and create accessibility. While hardware scaling is easy, software scaling, particularly biometric verification, is not so, especially in areas where connectivity is a problem. The technology is still being provided through the BC module and transaction costs are high. It remains to be seen whether such small value, large volume transactions will be profitable in the long term with such high transaction costs.
- Remittances: Financial inclusion is achieved through the BC module for cash deposits and cash payments. Remittances have yet to pick up. That will happen when there is acceptability and ease of process. Presently a lot of information about the beneficiary's bank is required. India being a cash-heavy society, individuals get better comfort by receiving their payment in cash. Banks need to work on QR situations and create awareness and confidence in the system among the people.
- Credit availability: This should be a very simple process. The back-end should be very strong. A huge database needs to be made available with a proper algorithm based on consumer behaviour and lifestyle, and not on their income. Mr Jain foresaw that in times to come, banking needs will be integrated with the e-mandis, e-trades and e-availability.

He concluded that financial inclusion is work-in-progress. As far as paperless banking is concerned, the technology is available and is an enabler, but adoption is a challenge. The country still does not have e-KYC or a centralised data repository. All the information in the public domain needs to be integrated. "Until all that data is integrated and we move to e-KYC and verification of documents through a system-base, till that time paper banking will continue," he said.

He was all praise for the authorities. "The regulator has done a lot of things as far as digital banking is concerned." He named several new initiatives that were put in place. As a banker, he said that their wish-list included innovation, supported with expertise finance and subsidy. Less cash in circulation will result in huge saving to the regulator as well as to the banks. Hence it makes a fit case to provide incentive schemes to consumers to use plastic and mobile phone transactions.

Ms Debopama Sen

Digital must create value for a bank's clients. "It is no longer about everyone is growing, and so no matter what you do, you will grow. Those days are all gone now," declared Ms Sen as she commenced her discussion about whether banks are doing enough to offer digital and technology to their clients. She described two or three things happening in the Indian context: in addition to the fact that Indian corporates are going overseas, the world of e-commerce has actually changed individuals' views about the kind of experience they should get. Technology was always available; but the expectation is now very different.

Today an individual can, at any time in the day or night, buy something online, pay online instantaneously and get instant fulfilment. Such an individual is more amenable to using that system in the office, and demands a similar experience. The biggest shift that the banks have made is that they are now looking 'customer in'. She explained: earlier, they were 'enterprise in', when they focused on what they could do and created something that they felt the customer could buy; now they start with the client, and create what the client wants.

She described an instance about the instant transformation of a Citibank client who was operating in 70-odd countries from India. One of their biggest concerns was opening accounts on a continuous basis. They were quickly able to adopt the bank's solution of opening accounts online completely without any paper except what was statutorily required.

Like retail customers, corporates too are now more amenable to using the technology. The buying centre is the corporate treasurer or the CFO; being very comfortable with the digital experience on the personal front, they are now demanding that at the workplace. And banks are catching up. Speaking from her own experience, Ms Sen said that in earlier years, innovation usually started in the consumer space and took about three to four years to enter the B2B space. That time is a matter of months now. She was of the view that UPI may have been originally set up for a P2P payment, but it will only be a matter of time before everybody starts using it for B2B as well.

Ms Sen also felt that UPI can make banking convenient and lower the cost of transactions. The most interesting thing about UPI is its simplicity, she observed. "UPI is refreshing in its simplicity because all you do need to know is somebody's virtual ID." It is a payment platform and a settlement mechanism. Eventually, she said, it will come down to how the banks and service providers build an ecosystem of useful apps around it; and how they are able to make it extremely secure and then bring that awareness to the customer. "The time for that kind of technology has definitely come in India."

In her opinion, a lot of banks have been collaborating very well with fintechs. Her own bank works with seven or eight such entities. "Fintech and banking have found a way to make 1+1=5," she said. But cyber security remains a concern. The banking and technology community have a responsibility to help their clients understand what end point security means for them. "Cyber security goes beyond technology into people and processes." Ms Sen felt that the banking community must instil confidence in clients. "That's a big factor in SME adoption as well," she pointed out; a small company that wants to explore digital will need help in making their environment secure to start believing in the technology. Banks are doing this all over the world. A lot of countries have also done a good job of digitising their cross border trade ecosystem and domestic trade. In her opinion, that will be another very important factor for India. The flow of documentation can become completely seamless and digital. The country has a long way to go in this, but strides have already been made. She predicted that this will be another area of hectic banking activity in the near future.

Mr Rajeev Ahuja

RBL, said Mr Ahuja, is a younger bank compared to many others, without the legacy advantages of entrenched customers. The entire industry is going through digital re-mastering at the industry and corporate level, after the success of Amazon and Uber. Eighteen months ago, RBL Bank decided to go onto an open banking platform, leveraging the power of API. API has been used for a long time, but it has always been internal to banks. In fact, he said, API banking or open banking is a platform that can be leveraged effectively to "allow quick, easy, and flexible access and innovation to be done not just within the bank but outside." He disclosed that they have a lot of developers who are using their ready APIs to innovate on the top.

Mr Ahuja affirmed that RBL Bank leads with API. Most of the bank's large clients are seized of the challenges of working in an extended enterprise where competition is also non-traditional. The bank has to engage with a million customers. They decided to invest in API and built their technology platform between 2012-14. "We didn't have to do a lot of messy wiring," he acknowledged, which would have been the case with older technology platforms. They used an ESB middleware to power the applications side of transaction banking. Payments, collections, MIS and account opening are all 'APIsed'. They will customise APIs and leverage their power, but will also ensure that they are available on tap, and build around them.

Mr Ahuja declared that he has a very high view of fintechs. Fintechs use public architecture and bank sponsorships to create point-to-point solutions. RBL Bank is one of the most prominent backers of fintechs to leverage their domain understanding as their banking providers. Fintech, he explained, is not only about technology; it is about having a deep understanding of customer pain points, or opportunities that large institutions usually gloss over, "where either banks have no access, don't have time or have forgotten them." One of the biggest opportunities for banks is to work with fintechs to co-create products and payment opportunities for SMEs and even MSMEs. "At heart, we are a fintech bank," he said, about RBL Bank. The fintech people have very good insight into using technology to solve problems. He strongly advocated partnerships with fintechs.

Banks are doing whatever they can to digitise transactions. There are two barriers to this. One is the internal barrier in the bank, due to organisational inertia. The second barrier is that banks try to fit solutions to existing situations. "We try to over-sell, over-engineer and do things which satisfy our internal objectives versus recognising that things exist for a reason." He described the debate about cash versus non-cash. "It's almost like saying that cash is bad." In his opinion, cash is actually very good and secure because India has not had access to modern financial services for a long time. The market will evolve with solutions that can capture social and commercial relationships which are already on the ground. Such solutions must be sought, especially for mid-size, small-size and really small companies and businesses.

Mr Asit Oberoi

Over the last 10 years, banking has seen a lot of electronification across the globe. Earlier, each bank had multiple peripheral systems to meet different needs. That is gradually changing over time. Electronification helps to have standardisation. Customers deal with multiple banks and would rather have standard procedures and protocols.

Corporates are very concerned about information security. They are rightfully paranoid about the security of their credentials and access to their bank accounts. They also want predictability of outcomes. Bank offerings have now moved in line with the customer requirements of standardisation, information security and predictability. Yes Bank has also taken to API banking in a big way over the last 18 months, Mr Oberoi revealed. Reconciliation is almost instantaneous. It leads to productivity benefit because during the festive season, hundreds of thousands of transactions take place. It helps banks and corporates move ahead significantly.

Today the talk is about API; tomorrow it will be about blockchain and other exciting things in the supply chain. Digital will make everything available to all parties of the channel finance transactions. "From a transaction banking perspective," he said, "an integrated solution is a Holy Grail that everyone is aspiring for."

Mr Oberoi predicted that with UPI coming in, a lot of cash on delivery on e-commerce will move to UPI since that will be convenient. But it cannot be overlooked that India is a cash-driven economy. Clients will always need cash. Hence Yes Bank has tried to digitise cash by offering something called 'Bank in a Box' which is placed in clients' offices. They can deposit cash at any time in the day, and it has been very successful in large places which deal with cash.

There are opportunities to do a lot more. Fintech looks at a specific technology or issue or a pain point. That is their core strength. The core strength of banks is banking. Yes Bank has multiple avenues for engaging with fintechs, said Mr Oberoi. It is an opportunity to create a win-win situation for both the bank and the fintechs. If the partnership is managed effectively, the fintechs market their products better, and the bank can address the pain points of the customers.

In the case of SMEs, as in corporates, one size can never fit all. A lot of fintech is coming up in the SME space, such as P2P lending. If a fully integrated solution can be created that takes care of the full banking of the dealer or supplier, it can be very useful for them. SMEs have a very small finance team; a lot of them use Tally. Yes Bank has a very good API-based solution which helps them significantly. If the finance functions can be made easier, banks can add to the growth of the SMEs.

A lot of change management is involved in preparing the mindset of the customer to move from an almost legacy system into an integrated system. It may not be the CFO's number one priority, since he has to deal with his own KPIs. Change management is quite intense; he may try to defer that decision. Data consistency is also a challenge. As banks migrate from multiple legacy systems into one integrated system, data consistency becomes important. Mr Oberoi was pleased to note that a lot of work is going on in the RBI on this front.

Customer needs must always be kept in mind when designing technology. Very often, observed Mr Oberoi, a technology company is given a requirement and asked to design it. "But if there is no input of what the client needs, then that experience is never going to be good." The design must be created with information about what the client needs.

Mr Abhay Gupte

The adoption of technology by banks is driven by four foundational components: convenience, speed, security and cost savings. At the same time, the quality of deployment can make or break technology adoption very quickly, particularly in the era of social media, when opinions can make a difference. These things will certainly matter as the next generation comes into the banking area in large measure.

There are three important aspects in the adoption of technology: The first is how the technology provider is able to innovate and bring in newer technologies; able to introduce newer areas of business; identify the risks; and have a mitigation plan. The important part is the ability to keep up-to-date with newer trends and newer areas of business. Every start-up is working on one part of the business and threatening the so-called legacy player. Banks need to adopt newer technologies and change. Speaking about his own organisation, Mr Gupte said, "We have, at the cost of reducing our revenue, replaced the technology or re-engineered the services to the client." There have also been cases where the service provider has disappeared, putting the bank or the corporate at risk. The longevity of the service provider is very important, especially in the area of transaction banking where large volumes, security and immediacy are crucial.

The second aspect in the adoption of technology is the ability of the provider to bring together multiple service partners and create an ecosystem which is healthy and supportive towards the bank. Gone are the days of a large system doing multiple things for the bank. Banks are keen to take on multiple products in the disruption that is occurring with start-ups. Restrictive technologies become a problem for buying and collating. "Banks are now taking those calls to work towards an open system," Mr Gupte observed.

The third aspect is how the technology provider is able to help the bank adopt the new technology. Learning systems and FAQs are crucial and become integral to the bank's ability to service clients. Adoption of technology, with all its complexities, is at different levels across the country, given the societal and economic differences.

There are three stages in financial inclusion: acquire, transact and engage. Banks have changed their methodology in each one of them:

- Acquire: Earlier the client had to walk into the bank and become a client. Now the bank goes to his doorstep and does his banking. The challenge has been to access the remotest part; that challenge is being addressed through technology. But equally, it is also a challenge to access busy, net-savvy clients and meet their expectations and needs from banking.

- Transact: Mobile wallets, fintechs, and Internet banking have made a difference. But the question is whether they have reached where they need to. Technology is making a difference, but is making inroads very slowly. Banks are working towards creating easy to use, low-cost technologies that are not just smartphone-based, but also feature phone-based.
- Engage: Engagement has not had much impact in the rural part of the country. In urban areas, social media and other areas of engagement have been effective in deploying newer products and newer areas of business. Technology deployment is still hardware-specific; that needs to change to open technology. Another issue is that in many areas, the sale of technology is time-based. For example a license is sold for a year. Mr Gupte suggested that the sale should be usage based; once that happens, it will have a much better impact, especially in the rural areas.

He submitted that regulators are doing a lot towards digitisation. But he advocated a roadmap over the next one or two years so that the larger ecosystem comprising banks and vendors are ready and will be able to adopt the changes much faster than they are able to do today.

Mr Kiran Shetty

One of the biggest things that is pushing digitisation is mobile or Internet penetration across the globe; that is only going to accelerate, stated Mr Shetty. He gave the example of a mobile wallet called bKash in Bangladesh. They registered about 20 million users in a very short time. They have been so successful, he said, "for the simple reason that they are simple." The product is very secure and can be operated from a feature phone. In India, the evolving infrastructure such as Aadhar and UPI are going to accelerate digitisation. These technological developments are further hastened by the many start-ups that are trying to provide innovative solutions to bankers.

Technology adoption by banks is a game of wallet share. The pressure in the ecosystem today leaves them with no choice. "The start-ups or fintechs are coming in with newer solutions." And banks have the will. "It is a universe of partnerships," he said, adding that the newer ecosystems that are being created will further accelerate it. He felt that the country in general and the banking fraternity are moving in the right direction.

Speaking about SMEs, he felt that one of their current challenges in using technology is the infrastructure that is available. There are bandwidth challenges. But that is evolving, and when it improves, it will definitely accelerate adoption at the SME level.

But, Mr Shetty cautioned, as digitisation gets accelerated in the Indian banking environment, there is a need for increased awareness of cyber security. RBI can play a role in disseminating that knowledge. He requested RBI to put in some controls and checks and balances within the ecosystem.

*(L-R) **Mr. Yashraj Erande**, Partner, BCG India, **Mr. Nitin Chugh**, Country Head – Digital Banking, HDFC Bank, **Mr. Mrutyunjay Mahapatra**, DMD and CIO, State Bank of India, **Dr. A S Ramasastri**, Director, IDRBT, **Mr. Sandeep Sharma**, Managing Director, South Asia, NICE, **Mr. Subir Mehra**, Global Head of Operations - Global Service Centres, HSBC, **Mr. Pankaj Sharma**, Executive Vice President, Retail Operations, Axis Bank.*

Session on 'Robotics and Artificial Intelligence: Ultra productive operations'

Session moderated by **Mr Yashraj Erande**, Partner, The Boston Consulting Group, India.

Panellists

- **Dr A S Ramasastri**, Director, IDRBT.
- **Mr Mrutyunjay Mahapatra**, DMD and CIO, State Bank of India.
- **Mr Sandeep Sharma**, Managing Director, South Asia, NICE.
- **Mr Subir Mehra**, Global Head of Operations - Global Service Centres, HSBC.
- **Mr Nitin Chugh**, Country Head – Digital Banking, HDFC Bank.
- **Mr Pankaj Sharma**, Executive Vice President, Retail Operations, Axis Bank.

Panellists' Views

Mr Mrtyunjay Mahapatra

For the uninitiated, robotic process automation is nothing but what it sounds. It is automation which is standardised and sanitised for all the possible risks that a machine can pose, whether it is a mechanical machine, a computer or a combination of both. Machines can learn how to behave in processes or situations that either do not require discretion or spontaneous decision-making, or are based on use cases. As far as artificial intelligence is concerned, studies of the human mind have revealed that human intelligence is not just intelligence, but a combination of past experiences and standard reactions of others. The machine combines such cases and produces the answers. These options are increasingly being put to use, although not on a very large scale. With such widely used processes, AI and robotics can be used to give a differentiated experience which is predictable yet coherent and robust.

The time has come for the banking industry to adopt robotics and AI. It will be a game changer in the next three to five years, Mr Mahapatra predicted. Currently use cases are being generated. State Bank of India, he said is trying to employ robotics and process automation in two areas: one is in its call centre, where 25% of callers ask technology-related questions. Those calls have to be transferred to the technology wing where someone else answers the question. The caller is asked to hold while being transferred to the technology team. This can be done by a robot. Reconciliation is another area. A huge army of people, disclosed Mr Mahapatra, work at the back end, trying to find reconciliation errors. The bank receives more than a million grievances every day. Most of it can be transferred to artificial intelligence.

He also informed that his bank has a 200-member team doing analytics. They have several gigabytes of data. But they need to make sense of it. In his words, "Data is the new oil, but I always say data is like crude oil because it requires a refinery to get the petrol and diesel out of it." He was of the view that robotics will be a game changer in the next three to five years. If even 20% of the inefficient processes can be made efficient with robotics, it will have to be done. But as in any transformative process, "adoption has to be driven from the top."

Given the specificity of Indian conditions, all the AI and robotics have to be largely home-grown. Based on his own experience, Mr Mahapatra had a word of advice for bankers: "The robustness of these programmes will depend on the quality of the in-house team that you put; the quality, timeliness and appropriateness of the technology you choose; and your ability to throw out things that are not working."

He was asked what it takes to be ready for these initiatives. "Readiness is a journey," he said. There is no absolute state of readiness. He considered the example of data and analytics. Today, no organisation can do any work in artificial intelligence or process automation based on own data. They have to be prepared for big data. Big data is own data which is structured, as well as data from various sources that may be in a different structure. That ability to get data from diverse and unstructured sources, analyse, process, stage and store it is the first requirement. Next is the preparedness of the people involved. Banks in India are delivering technology from locations which are geographically, culturally and demographically different. These capabilities have to be taken to the frontline so that people there are able to use and adapt it. And the third point is choice and prioritisation. It is quite likely that AI and robotics process automation may have to be retired in the next 12 to 18 months, with new technology coming in. Selling it internally and convincing decision-makers that this is required, even with a high rate of failure, is a challenge.

Artificial intelligence will co-exist with natural intelligence. Hybrid is the way to go. The challenge will be to get the right blend. This blend will differ from customer to customer. It is very difficult to get to an ideal state before we start. In today's world, with the pressures of competition, there will have to be some experimentation. The ideal state where employees will be completely skilled with all processes defined before implementing robotic process automation will never be reached. What should be defined is the risk appetite, where to stop, the amount of reputational and monetary loss and when to set the process to rest. All this must co-exist and function together with cyber security. Technology and competition are changing fast, and there will be a lot of opportunities. "If you don't catch it, it won't come back," Mr Mahapatra counselled.

Mr Sandeep Sharma

Mr Sharma began by asking for a show of hands: "How many of you have used Yellow Pages or a directory in your life?" He continued, "How many of you use Google today?" He explained that when somebody looks through a directory, it is a manual effort. All that effort is now automated using Google. Artificial intelligence comes in when Google learns to predict what the user is searching for. While artificial intelligence is still maturing, robotic process automation, he said, is here today, across all industries. It is critical for banking to adopt it.

He described some of the use cases that work well with these technologies. One of the most common themes that resonates very strongly across industries is digital. In the Indian banking context, there is still a lot of paperwork involved; that is a big hindrance. Globally, across industry segments, wherever there is a lot of digital content, such tasks lend themselves dramatically to robotic process automation and artificial intelligence.

Mr Sharma divided customer service into digital and assisted channels. Digital channels could be smartphones or websites. These channels are now becoming the preferred mode of interaction for consumers in the country. They don't want any human touch in these digital channels; they want it all to happen automatically. Even on the assisted channels, individuals don't like speaking to robots. In the future, he felt, they will be talking to humans, as will be necessary in scenarios that the digital channels cannot address. Individuals manning assisted channels must be very capable of supporting whatever business problem they are given. They don't expect robots to know all the permutations and combinations of possible solutions. "It is really about digital," he said.

Cyber security is a legitimate concern. These technologies are complicated, with millions and millions of lines of code. Especially in the banking sector, there is very rigorous testing before the software is deployed. "At the end of the day, it is all about risk." The question is whether there is less risk with humans, or with robotics process automation. The case studies generally suggest that the less the human touch, the less the fraud capability. But it cannot be zero. There definitely is risk. Information can be hacked; but at the end of the day, a combination of rigorous testing and quality software precludes the chance of that risk being very high.

Mr Nitin Chugh

Robotics automation has been around for a long time. It is not new as a concept but it probably means different things for the banking and financial services industry. The industry has generated a lot of data, half of which was generated in the last 10-12 months. "How do you make sense out of the data?" asked Mr Chugh. That is where, he explained, some elements of artificial intelligence and robotic processes come in, to analyse the data and put it to use in processes which are more repetitive in nature. Artificial intelligence is developing almost like a layer on top of the existing set of intelligence. "The fact that Google can tell us what we're looking for and tell it very intelligently is because it's also assimilating a lot of information about people who are using Google. That wasn't the case when we didn't have Google," he observed, pointing out that if a person looked up the Yellow Pages, only the user knew about it and it did not matter to anyone else. Today, with artificial intelligence, even the subject of the search knows that he has been Googled.

He shared the methodology that is being followed at HDFC Bank. In one use case, they break up the lifecycle that a customer logically follows with the bank into three or four parts; for everything they do, they keep the customer at the centre, so they are very clear about the customer impact. They visit the interventions and conversations that the customer has with the bank across various channels, and then examine how much of that can be made more intelligent. Everything may not need to be replaced by robotic processes; but the agent who is handling the customer can be assisted by a robotic process so that the query is resolved upfront. He explained that an agent in a call centre may or may not be equipped to answer a particular query. The same query can be handled very promptly if there were a robotic assistant to the agent.

Another use case is for routine matters dealing with queries and content which could be either on the website, in the contact centre or even in a branch. Some of that content is readily available, and easily converted into artificial intelligence-based robotic processes in which the customer finds value. The third use case is going into the whole area of carrying forward the trust that the customer places in the bank. In Mr Chugh's opinion, "there is a very bold line between convenience and trust." The bank may feel that it is making things convenient for the customer, but the customer also needs to trust that service. One example of this is the robo-advisor which is a software programme that advises customers on their investment needs. The customer should be able to trust that robot; but more important, that trust should happen because the customer trusts the bank. That is the way the relationship should evolve.

He clarified that these use cases are based on the customers' point of view. "There are as many or probably more when you look on the internal processes side." He was clear that it is equally important for the bank to make sure that it does not only increase convenience and access for the customer, but also translates that same thing into a heightened level of trust. The internal processes must be addressed first, and the enterprise and employees must be ready to handle it. Only then should it be brought into the domain of the customers. He was not in favour of exposing customers to something that is very new, for which the organisation itself is not prepared.

Mr Chugh also discussed how they source the talent needed to work with data scientists, robots and humanoids instead of branch managers and credit officers. He said that there are very few cases "where you will have a robotic process replace a human being, and that might happen in something which is repetitive." Anything which is more conversational requires interactions and some degree of understanding emotions. He visualised a situation of co-existence rather than replacement. An agent handling customer calls may have a certain manner of responding to the customer, retrieving information and following a laid-out process. That agent must co-exist with a robotic assistant that is also assisting the agent in improving her response to the customer. It is about two different elements existing together rather than the robot replacing the agent. The bank's people need to be re-skilled from that perspective.

Mr Pankaj Sharma

Mr Sharma was asked why robotics process automation and artificial intelligence are important. In response, he gave an analogy: around the year 1700, nobody thought about the way they could work. There were no factories, and everybody did manual work. In 1710, the steam engine was invented. It led to the Industrial Revolution. It brought about a change in mindset. "Now," he declared, "after 300 years, we are at the cusp of the Artificial Intelligence Revolution." He felt the use of AI would be multi-fold.

Large organisations need to be clear about how they implement artificial intelligence. There has to be a planned approach. The organisation should be clear about its business operations and digital strategy. The transformation should be around that; unless the organisation has a good understanding of what it wants to do, it will not be able to deploy these technologies. Improvements should then be brought about through engineering efforts like six sigma innovation. One the organisation reaches this level of maturity, introduction of artificial intelligence makes a lot of sense. The next level of improvements will only come from AI and robotic processes.

AI and robotics can be used across all functions of the bank. At the front-end, it can be used for target segmenting of customers. At the back-end, cheque processing and reconciliations can be managed. Axis bank has even automated simple processes like account opening. Mr Sharma explained that although e-KYC has been launched, its usage varies from bank to bank, and overall it is not being used beyond 10% by the industry. In order to address the remaining 90%, Axis bank has used software bods to create straight-through processing for tablet users. Using this, they can open an account for 40% of their customers who use tablets in less than 15 minutes. In the area of support functions, AI can be used to answer some queries. A lot of employees keep sending emails to answer questions that are repetitive. AI can be deployed to answer those questions. Axis Bank is also using it in their call centres to do sentiment analysis on irate customer calls, to bring in real time intervention where a supervisor can intervene and handle the call better. AI is also being used in a big way in analytics.

The right starting point for RPA and AI is to identify the manual part and automate it. Readiness for these initiatives is directly related to the passion in the organisation to do something new. He alluded again to the analogy of the Industrial Revolution. "Before that, no one had actually thought that we can change the way the factories work." Similarly, he said, today's organisation can continue with the present way of working; but as the world moves ahead, if the organisation wants better margins and cost income ratios, these elements have to be evaluated.

He underlined three categories of challenges in the Indian context. The first is the technology itself. Today, there are very few product-centric solutions. The banking and financial services space has got lots of options for customisation. They can either work on a productised approach where the options are limited; or they can collaborate with start-ups who are working in this area. It involves time and investment, but it can achieve breakthroughs that may not have happened anywhere in the world. The second is process risk. This is very important because banks cannot afford to have type 1 errors or work on false positives. The reputation of the bank is also at risk. To gain the customers' trust, banks should be sure of the processes they deploy at the back-end. The third kind of challenge is the most common: it is the entire human resource angle where everyone fears job losses. Mr Sharma felt that a lot of the banks and NBFCs in India are entering a retail space, where he foresaw a growth of 25%-60% in the next few years. "A lot of these deployments can actually help us in getting those efficiencies which will help in managing this rapid growth with the same set of people," he said. He called for a proper balance between the combination of human and artificial intelligence.

Mr Subir Mehra

Mr Mehra was of the view that artificial intelligence and robotic process automation is very important for banks. Manufacturing companies today cannot run without thinking seriously about robotics. This is because margins have got so compressed that they need to keep thinking of ways to cut costs. Similarly in banking, it is becoming very difficult to make money. "Interest rates today in most of the western countries are now at zero or even potentially negative." He continued, "It is a challenging industry to make money and if we don't start thinking about innovative ways to start looking at our costs and our productivity, survival itself is at stake." Hence, he felt, robotics is an extremely critical area and the advantage that banks have is that a lot of the technology for robotics is already available from multiple, well established players. It is a game changer that can increase productivity and cut down errors. Banks that are not using robotics today should be asking themselves why they are not using it, he said.

Mr Mehra said that any use case in which a process can be mapped and it can be defined where a human being is doing a task where a decision is not needed, lends itself to automation. If some sort of judgement is to be applied, then it becomes very difficult to implement RPA, and artificial intelligence may come in. By way of example, every bank receives thousands of emails. Not a single one of them is structured. Hence it requires human judgement to be able to read an email and understand what the customer is asking and then provide an appropriate response. This type of task is not conducive to RPA. If at all it has to be automated, it requires significant investment in artificial intelligence. On the other hand, banks look at the annual reports, financial performance and ratios of companies to make lending decisions. HSBC uses RPA technology to read the annual report of a company. It maps all the financial data onto Moody's format and even captures the information about the customer into Moody's database. It extracts from the database the ratios of the customer compared to other companies in the industry and enables the bank to make a good lending decision. Earlier, this activity was fully manual. Today, the number of people required to do this task has come down to 15% of that originally needed. "There is no judgement here," Mr Mehra pointed out. "This is just about extracting information in the format that can be put into a Moody's database." Even within a process, he said, if it is mapped out step by step, there may be 30 steps out of which 26 are completely manual with no decision requirement. Those 26 processes can be automated. "You don't have to necessarily automate the entire process, end-to-end."

He was categorical that automation would not lead to job losses. It will only mean that the kind of work that people are doing will improve. Banks, he pointed out, are hiring graduates from good universities to do basic jobs such as getting a company's sales number from an annual report and keying it into Moody's database. They must now get into newer areas. They are at the forefront of fighting financial crime. The kind of people needed for that activity is exactly the same as those who are doing basic manual work today. They are good quality, intelligent graduates. "As we automate, we have the ability to redeploy people into much more value-added activities. But there is a challenge: these people have not been skilled to do that kind of activity. Banks need to invest in training. Equally, he said, the managers who supervise these people were never trained to manage a workforce that does a lot of judgemental work; hence investment has to be made even in training managers. "At no point in time have we considered that this is going to be causing massive job losses."

Dr A S Ramasastri

"It is very difficult to define what artificial intelligence is," began Dr Ramasastri. The word 'artificial intelligence' is used more in universities and academic institutions because there they are trying to mimic what intelligence is and give it to machines. Once the machine starts using it, industry uses it as part of its product. What was considered to be artificial intelligence a few years ago may not look the same today. An example he gave was patent recognition, which was seen as artificial intelligence about 15 years ago, but is taken to be a normal product today. Artificial intelligence is already being used in many sectors and to some extent in banks also.

As for robotic process automation, he said, the word 'robotic' is used in a different context here. Robots are understood as mechanical. Robotics is used in factories and even in hospitals. When it comes to banks, robotic process automation refers to things which are done routinely. But there is some more important work going on. "Is it possible that the robot really comes and does some of the things that are happening in the branches or elsewhere?" he asked. He gave other possibilities: could the branch have a helpdesk which is like a robot, or can call centres be equipped with a robotic voice, he wondered. "Siri today is an acceptable thing," he pointed out; it can understand speech and mimic voice. "Maybe, that is a type of robotics that can come into the banking industry also." But he cautioned that manpower requirements and costs have to be looked at. Sometimes, predicted outcomes may not happen. The industry must weigh each of these factors. Robotics, process automation and artificial intelligence are all equally important and very useful.

The industry is ready for the technology, he said. "We are not lagging on the technology front." He also felt that the industry is moving ahead on the data front, by setting up data warehouses. The new banks also have data without the baggage that the older banks have. But what will bother most banks is the skill set. There are new designations like 'Data Scientists' who need to be introduced into the system. If the people already in the bank are not fully comfortable with the new system, the overall confidence level of the bank will not be as high as it should be. To get that level of confidence, a reasonable number of people should be able to adopt the new system. This will take some time. "People are the most important thing," he believed; process can be redesigned, but the willingness of people will come with comfort and confidence in the system. Advisory services can be used, but there again, a lot of trust is required not only internally but even outside.

Core banking implies that payments are done in the cyber world. The security for that is already in place. If artificial intelligence, which is being used to track transactions everywhere, is able to identify and put out an immediate online alert about a threat, that will be useful in detecting transaction frauds. Such a system can be used as a defence against cyber attacks. Once an alert has been sounded, human beings will have to decide whether to act on the alert, and what action needs to be taken. That is judgemental and will still remain with human beings. Hence, artificial intelligence should be viewed in the proper context. It can substitute some of the processes and intelligence that human beings are able to use, and be more useful to those same human beings. It will be an enabler and facilitate tasks being done by people. But human beings will not be able to transfer all their intelligence to machines. "At no point can we say that we will completely transfer all our intelligence, but we will make it more and more intelligent than what it is today," he concluded.

Summary by **Mr Yashraj Erande**

Mr Erande began by asking whether artificial intelligence and robotic process automation are the same, or whether they are different. After hearing from some of the panellists, he inferred that "process automation is about taking a set of tasks and doing them using a machine or a robot instead of a human; and artificial intelligence is about using information data, signals, to build algorithm heuristics that can help make sense out of it." He asked for an audience poll on how many of them believed that RPA and AI will be game changers in banking and financial services in the next three to five years. The options he provided and the responses in their favour were:

- Option 1: The impact will exceed our expectations; it will be dramatic and we will not recognise the way we conduct our operations. Operating models will change fundamentally.
  - Responses in favour: 1%–2% of the audience.
- Option 2: There will be some impact, but the current way of working cannot be written off in the next three to five years. It will still remain large, dominant and relevant.
  - Responses in favour: There was a larger bias towards this option.

With this context and feedback, he proceeded to examine why RPA and AI are important. He conducted another audience poll: Since the amount of capital that gets deployed for any technology or innovative idea to become mainstream is a very important metric of success, he asked the audience what investment they believed had gone into RPA and AI in 2016.

- Option 1: $ 1billion, which means it is still early days by global standards.
  - Responses in favour: Three or four.
- Option 2: $ 2–3 billion, which is still substantial money by any standard.
  - Responses in favour: Majority of the audience.
- Option 3: Excess of $ 4 billion which is the market cap of the banks that exist in India.
  - Responses in favour: About 20.

He revealed that the investments cumulatively as of now stand at $ 4.1 billion. There are 140 companies across categories that belong to the broad umbrella of RPA and AI. "Clearly," he said, "providers of capital have not shied away from deploying a lot of effort and energy behind RPA and AI."

He proceeded to ascertain from the panellists the importance and criticality of this technology for financial services in India, and get an insight into the use cases that actually work. He then explored what it takes for an organisation to undertake this journey successfully, and asked for a show of hands from the audience about the readiness of Indian banks and non-banks to undertake this journey of greater productivity, certainty and customer convenience, by using technologies around RPA and AI.

- Option 1: We are fairly placed as an industry to capitalise on this opportunity.
  - Responses in favour: A small number.
- Option 2: Respondents are optimistic, but there is still some ground to cover to get there.
  - Responses in favour: A larger show of hands.
- Option 3: We're just beginning to scratch the surface; in other words, we are still in the dark ages.
  - Responses in favour: Inconclusive.

He concluded that there were quite a few 'none of the above' members who were holding back their opinion. He summed up the view of the panellists about readiness: it involved the ability to deal with data; minimise risk by getting the process right; and integrate the new methodology into the ecosystem. He reiterated that "some of these technologies are so cutting edge that you will need to learn to work with people and partner with them and outsiders to make this happen."

Before he threw open the subject for discussion, he went back to his first question to see if there was a change in the opinion of the audience about whether RPA and AI will be a game changer. Their response convinced him that the panel was able to transmit its thoughts to the audience successfully.

*(L-R) **Mr. Amit Kumar**, Partner, BCG India, **Ms Rajkamal Vempati**, Head - HR, Axis Bank, **Mr. Ashwini Mehra**, DMD & CDO, State Bank of India, **Mr. Sushil Muhnot**, CMD, Bank of Maharashtra, **Mr. Amitabh Singh**, General Manager – HR, ICICI Bank, **Ms Vibha Shukla**, Director & Head - HR, SAP India Pvt. Ltd.*

Session on 'New performance paradigms: Getting used to highly transparent and measurable world'

Session moderated by **Mr Amit Kumar**, Partner, the Boston Consulting Group, India.

Panellists

- **Mr Sushil Muhnot**, CMD, Bank of Maharashtra
- **Mr Ashwini Mehra**, DMD & CDO, State Bank of India
- **Mr Amitabh Singh**, General Manager – HR, ICICI Bank
- **Ms Rajkamal Vempati**, Head - HR, Axis Bank
- **Ms Vibha Shukla**, Director & Head - HR, SAP India Pvt. Ltd.

Overview by **Mr Amit Kumar**

"We are having this conversation because I think there has been a lot of discussion in the banking industry and also in the economy about how we are thinking about performance management," began Mr Kumar. Performance management is a very important lever of performance; it tends to be a topic where people have a very strong point of view. Often, the organisation is trying to figure out whether its current model is working, or needs to be changed. If people within a bank are asked how satisfied they are with the bank's current performance management system, more often than not a large number will say that it leaves a lot to be desired.

A buzz word often used in the industry is 'bell curve'. "I don't think performance management is about figuring out which curve you will use," stated Mr Kumar. If performance management has to deliver for the employees and the organisation, he explained, "then it has to be much more than what curve you end up using."

In organisations that get their performance management system right, line managers play a very important role in HR. "HR is far too important to be just left to the HR department." He explained that it is true that the HR department has to play a very critical role; but often line management has to come in and take ownership for what is happening with performance management, as well as with other HR decisions in the company. Often, a lot of line managers are woefully underprepared for this role. While a lot of investment goes into training people, that training is focused primarily on new products, new policies and market realities. It is very rare to find organisations training line managers to have HR discussions with their teams. "That is a very important element which organisations have to get right if you want this to work," Mr Kumar asserted.

The public sector is very different from the private sector, he observed. That acknowledgement has to be at the centre of any system that is designed. There tends to be very heavy grade inflation in a lot of public sector banks. There is also a culture of not giving feedback; a lot of managers will hesitate in giving tough feedback. Often, these systems are underprepared. IT can deliver systems; but frequently, even if there is a desire to start tracking a matrix and use it for HR discussions, that system is not in place because no one has demanded it.

For a new performance system to work, technology has to be brought in early on. The IT department has to be brought in upfront because as the process and decision system becomes more objective and data-based, all the different systems that capture data within the bank will have to get integrated.

Quoting from reported data, Mr Kumar informed the house that in the private sector, about 75% of the people feel that seniors whom they report to take the time to groom the team. In the public sector that figure is about 67%. He said, "Everyone who is not getting the grooming on a day-to-day basis typically is not performing to his or her potential." An organisation that wants to make a difference must ensure that its line managers step in and play a role. People often worry whether a new performance system will have the fairness they expect.

"The beauty of subjectivity is that it is hard to argue against it." The moment an objective system is in place, the first question is whether the targets were set fairly. A lot of energy and investment must go into ensuring that the targets are set scientifically and communicated to the organisation, branch managers and people within a branch in a way that they feel that the targets are fair and achievable with hard work. If they feel that the targets are unfair and cannot be achieved, then it will be difficult to discuss performance management with them.

If an organisation has, say, five zones, it must determine how the different zones are given different targets. Many organisations tend to give flat targets. Geographies that have a lot of potential will achieve them; but those that don't will not be able to deliver despite their best efforts. The latter will very quickly lose faith in the new performance management system.

On the bell curve, the performance differentiation within an organisation depends on what the organisation is trying to achieve in the next two to three years. There is no right answer. A public sector bank may choose low differentiation. Even with low differentiation, the organisation may choose to push a lot of people into the middle bracket to incentivise them to make it to the top. There are organisations that prefer 'meaningful differentiation with a positive skew', with about 60% in the top bracket, 30% in the middle and 10% in the lowest bracket. Then there are those with very heavy differentiation where the entire organisation is divided almost into three equal buckets of 1/3rd each. What Mr Kumar felt is important is that if an organisation does not have any differentiation, then the bank, the employees and the customers suffer. But he was very clear that "differentiation cannot be only at the time of promotions."

Today, with the kind of technology available, there is a move away from discussions being recorded in large files. Progressive organisations are beginning to move towards a 'tablet2tablet' review. Both parties carry their tablets to the review and use an intuitive interface to determine how they are doing. In many cases this is done on a monthly or fortnightly basis. Technology can even capture inputs that influence business outcomes such as how many customer meetings the employee held.

In order to design a high quality performance management system that can deliver, the organisation needs to spend time thinking about fairness in the system and in the minds of the employees. There should be consistency in the measurement of performance of different zones, or the performance management system used from year to year. A lot of organisations think of performance management only from the perspective of what the corporate centre is keen on getting, and distributing rewards. "The development agenda of employees has to be a very big part of the performance management system," Mr Kumar maintained. Energy must be invested in using the information being generated by the new system to ascertain how to groom and coach managers.

But, he pointed out, it takes time to implement a new system. There has to be a plan around it. HR departments need to be empowered so that they can start thinking about the consequences of non-compliance. "If the design is great and the HR department does not have any teeth in getting it implemented, then more often than not it will start running into roadblocks." He ended with a quote from President John F Kennedy: "There are risks and costs to a programme of action. But they are far less than the long-range risks and costs of comfortable inaction."

Panellists' Views

Mr Ashwini Mehra

For quite some time, State Bank had a one page appraisal which consisted of a number of parameters. People got graded from 'excellent' to 'below average' or 'needs improvement'. The supervisor gave some general remarks which were generally full of praise. The bank was not able to differentiate between the people who were being rated. They decided to come up with another system comprising 35 parameters on which employees were given marks adding to 100. In almost 90% of the cases, people ended up getting the full 100 marks. Again, they were not able to differentiate. Differentiation "possibly got forced only at the time when the promotion exercise was taken up," Mr Mehra admitted candidly.

A couple of years back, the bank decided to explore how technology could be leveraged to create a system whereby the performance of the officers as well as the clerical staff could be differentiated. All the possible roles were drawn up and divided into three categories of 'budgetary', 'measurable' and 'non-measurable'. The 'budgetary' and 'measurable' roles covered about 90% of the officers and clerical staff. Data for the budgetary roles was drawn from about 51 systems. From these, data was drawn up to populate the key responsibility areas that were earmarked for each official.

The bank now has a library of about 5000-odd KRAs covering about 1.7 lakh employees. About 70% weightage was given to their performance coming from the system. There were challenges with the technology, dissemination of information and the level of communication required to make sure everybody understood their responsibilities; as well as in ensuring that the exercise was seen to be motivational for people to try and improve upon their performance. "The journey has just begun. We are still grappling with a fair number of challenges," said Mr Mehra. But he expressed satisfaction that for the first time they are able to differentiate the performance of their officers and staff. "The differentiator that we have today is far more meaningful than what we have had all these years."

He also explained that performance differentiation works with a carrot and stick approach. That has been built into the State Bank system as well. If somebody consistently fails to perform, they have to face penalties, including cessation of service after a particular period. On the reward side, they floated the concept of ESOPS. Mr Mehra stated that State Bank is the first public sector bank to come up with their own proposal which is at present with the Banks Board Bureau and the Ministry of Finance. The idea was to incentivise those who did very well, and create a competitive spirit within the organisation for people to improve their own performance to get into that bracket where they get performance-linked incentives and ESOPs.

Mr Mehra also said from the previous year's experience, that if they run the performance matrix based on the scores that people got, it actually results in a bell curve. "So it does exist." They propose to provide consistent feedback to people on how they are performing against their KRAs. "They know in which area they are deficient, which area they need to improve and how they are doing vis-à-vis the people who are in a comparable cohort." The KRAs have been driven down right to the last employee in the branch. Targets are differentiated depending on their area, their geography and the potential in that region, to create realistic KRAs. The branch manager and his team get rated according to the performance of that unit. All of them work together as a team. Hence the bank is trying to improve productivity in the organisation, as well as assess the training needs of a particular unit. Exceptional performances can be carried forward to a more responsible role.

Mr Sushil Muhnot

One of the big advantages of the public sector is that the HR person is always a business person. He may not know much about HR, but he always knows business very well; and he is also part of the corporate planning exercise. Public sector banks also set targets. If those targets are set on a scientific basis, differentiation based on performance can be achieved. But most of the time, what happens in the public sector is that the baseline itself is low. Growth is expected from that low baseline at the same low rate.

Speaking about the bell curve, Mr Muhnot said, "In the public sector, the bell curve always starts from good, very good and excellent. There is nothing on the other side of it." On the whole, differentiation is low in terms of performance measurement. When the Government prescribed a minimum of 60% to qualify for promotions, most of the people got above 60%. When the guidelines changed to 75%, then almost everybody got above that grade because everyone had to be considered for promotion.

"To make it better, you must have a good carrot and stick approach," he felt. He noted that some incentive structure has come into the public sector. The incentive could be 5%–10% of the salary. As far as the stick is concerned, he informed that the Government of India has stipulated that if the organisation deems that a person has not been doing well, that person can be retired at that age of 50. He admitted that these initiatives have not been implemented widely, but a beginning has been made.

Banks always desire that 70% of the assessment should be quantitative and 30% qualitative. This is a challenge in service-oriented roles where the employee is not playing a business or operational role.

Mr Muhnot also touched on the subject of recruitment. He recalled that the Supreme Court had stipulated that the public sector is not allowed to take up campus recruitment. Initially, the public sector decided to have a written test; the decision now is to ask selected candidates to go for a one year post graduate diploma in banking and finance before joining. In this manner, even if they are not able to recruit people from the campus, they can get trained people to join.

The public sector gets very good people at the clerical level. They can be given more intellectual and analytical work. Bank of Maharashtra has recently started recruiting B Sc Agriculture graduates in Class III, which is the clerical cadre. They can become agricultural clerks or get six months' legal training and then join the bank. There have been challenges at every stage. But because of those challenges, there are also opportunities to implement those changes. He was confident that they will be able do it as competition in the sector increases.

Mr Amitabh Singh

One of the norms initially set by ICICI Bank is that performance assessment will be a boss's call. There will always be a certain amount of subjectivity involved. "Our job is to limit and minimise the subjectivity so that it is not ad hoc," Mr Singh clarified. "But," he continued, "there will always be a five or ten per cent call which the boss will have." He averred that over the last 20 years of experience, he had never found an organisation where a boss and subordinate could agree on the targets. Hence target-setting would always be top-down at ICICI Bank. But they were being realistic in setting targets. The key challenge they face is that while it is relatively easy to assess branch managers or people in sales because their results can be measured quantitatively, they spend enormous time setting targets and making the process transparent for people in non-quantitative roles. In such cases, their alignment with the business goals is assessed.

The other area where they spend a lot of time, he informed, is in building analytics around people's performance. A lot of work has gone into removing bias. Mr Singh explained that they have a series of 12 bias checks that are done while the performance management is on. Until six years ago, this was done post-assessment, followed by corrections. But over the last three years they have been getting so much real time data that the bias check is done during the performance assessment itself. The moment a rating is submitted, there is a system that identifies which biases had crept into the assessment and the rating is immediately corrected. They also do post-evaluation feedback; once the ratings are announced, they put up a call centre, manned by HR managers, where any employee can raise a concern. If the concern is found to be valid, the rating is changed. Such grievances have come down drastically over the last three years, he observed. Using this methodology, they have achieved about 95% correlation between the BSC score and the performance rating.

Referring to the bell curve, Mr Singh pointed out, "the moment you do a distribution curve, there will always be some people who will be at the other end." At ICICI Bank, they are not called 'poor performers'. They are simply described as 'not meeting expectations'. They are given time to remedy their performance. "In ICICI, you cannot ask any person to go unless the person has spent at least two years across any level." If the person consistently does not meet his target, the organisation realises that he is not cut out for the particular job and needs to look at something else either within or outside of ICICI. "But you cannot sack a person in ICICI by labelling him as a non-performer."

The belief at ICICI Bank is that both top performers and people who are not meeting expectations can improve their performance if they are ambitious. After two or three years, people are asked if they are actually doing the work they want to do. "It is a myth that in the private sector people are sacked," he said. Managers tend to be very benevolent towards those who report to them. They start putting a context to the performance. He actually advocated a boundary condition that a person cannot be sacked on performance. Banks will then be able to take more accountability on developing their team members.

Mr Singh also addressed the issue of 360o performance review. "Conceptually 360 cannot be used for performance," was his view. It can be used to estimate potential. In performance assessment, the boss has the most critical and the largest view of how the person is performing. This view is facilitated by data in a branch or sales job, and is more subjective in non-measurable roles. If several people have a view on someone's performance, it tends to become a populist exercise. The idea of a good performance management system is to improve performance.

Ms Vibha Shukla

Ms Shukla began by candidly observing that no employee ever agrees that her or his company has a perfect appraisal system. An organisation must recognise the need of the hour and define the kind of performance appraisal system that it wants. She felt that no system today follows a perfect bell curve. Interestingly, she disclosed that at SAP, they are completely eliminating performance ratings altogether. At the time when they did have performance ratings, the rating by the manager was followed by a calibration process where the person's performance was calibrated against the people in the department. Today, they are moving towards eliminating the whole process altogether. They are doing a pilot phase, she said, with a cross section of employees across geographies and various functions.

The reason why SAP is moving in this direction is because they believe that if they have hired an employee, they are obliged to offer that employee development opportunities to perform to the best. Otherwise, Ms Shukla pointed out, employees just work towards their own KPIs and compete with each other rather than try to collaborate and bring in innovation. For an organisation in the IT sector, innovation is extremely important.

So although they are eliminating the performance rating, they are doing something called the 'SAP Talk', where a manager and employee have focused quarterly conversations about the job, development opportunities and what help is required. That whole conversation is captured in their cloud- and harness-based SuccessFactors system. The system is intelligent enough to pick up repetitive words and generate a summary. It highlights the areas of development and the quality of the overall relationship.

There are, of course, challenges. One is implementing the system across various cultures. "In India," Ms Shukla observed, "we are not that open with giving feedback even at home." The cultural mindset has to be changed so that employees can receive feedback with trust that it is for their well-being. Similarly, managers have to learn to give feedback in a positive manner without offending people. The other challenge is in dealing with low performance. That is relatively easy with a ratings system. In this new concept of handholding, the manager is the first point of contact and has to ensure development. The challenge is to ensure that even the bottom performers start performing better.

"The conversation has to be developmental in nature." Instead of triggering an immediate performance improvement plan as is done in IT companies, they handhold the person, allot mentors and seniors to help the transition to the next level. It happens through guidance and coaching. "There will still be people who do not move up to the mark." The company has to take a call about those situations.

Ms Shukla also elaborated the process of 360O performance assessment. "In SAP, we use 360O, but it is only for developmental purposes. It has nothing to do with performance." It is encouraged at manager levels and above; it is upward feedback which is very important for the development of managers and leaders. But it is not mandatory; it is a choice for people in managerial roles, and for some in individual contributor roles. It is suggested when development discussions with the manager hit roadblocks regarding areas for improvement. The team gets involved and the employee chooses the peers who are to give their feedback. The feedback is not just about improvement; it is about strengths as well. It is presented as a consolidated report without the names of the people. It is then up to the individual to choose the areas to work on in the immediate future.

Ms Rajkamal Vempati

Ms Vempati began by demolishing two myths:

- Myth # 1: There is something called meritocracy.

Employees and managers both seek meritocracy. But according to Ms Vempati the concept is a myth, because while employees seek meritocracy in the form of differentiation based on merit, managers avoid it because it is the hardest part of their job. "Differentiation is the hardest thing and that is at the centre of the conversation today." It is the basis for any assessment. She examined why differentiation is required. It is required (a) for human motivation, and (b) because there has to be some reward distribution process.

Ms Vempati described the various phases that Axis Bank had in their journey of embedding meritocracy. At a certain point in time, 75% of its people were given the top two ratings; and the requirement from the managers was 95% to 98%. Data from the last 20 years showed that if 95% of the people were ranked in the top two ratings, the demand would be 98% or 99%. The aspiration is always higher than what was projected on the curve, and that was the challenge and paradox of what they were trying to embed. It was hard for the managers, but also critical to embed that philosophy especially since they were embarking on a cultural change.

- Myth # 2: Absolute assessment is fairer than relative assessment.

Bankers keep talking about absolute assessment. The data shows that budgetary roles are always differentiated. In qualitative roles, the dispersion is always narrow, and gives scores between 97 and 100 in most cases. It does not mean that a branch staff customer service officer who scores 99 must necessarily be placed in the topmost rating. Ms Vempati's argument was that relative assessment is fairer, because it spurs on employees to at least question whether or not their targets are achievable. Absolute assessment, on the other hand, promotes underachievement.

Ms Vempati then revisited Axis Bank's journey in performance management. The first phase of the journey was an era where they had a common reward system and a flat or broad differentiation philosophy. KRAs were accompanied by BRs which were called basic responsibilities. The input and output measures got mixed, which led to limited dispersion. Seventy five to eighty per cent of the people got assessed in that manner.

The second phase saw meritocracy being embedded as a concept. The bank tried to implement sharper differentiation. But the challenge remained the same. The demand from the managers was always more than what the performance curve projected. The bank began differentiating on the promotion process, recognising that differentiation needs to have adequate awards and rewards which are finite. Those who were placed in the top two ratings got promoted, say, in three years' time. Promotion was seen as the most visible indicator of performance differentiation. That was germination of the first seed of thought about meritocracy among the high performers.

In the third phase, the bank started differentiating a little more sharply on the variable pay and increments. But there were still questions about how they were managing differentiation, because the concept is associated with the tag of 'winners' and 'losers'. The bank recognised that performance will be volatile. It cannot be codified and made algorithm-based.

They have now embarked on the fourth and current phase which is more inclusive. People are bucketed broadly into three pools. The bottom-most performers are called the 'enhancement pool people'. They are given a window of possibility. They have six months to rectify their performance. In qualitative roles, they are given a stretch target, and in quantitative roles, they are required to do a little bit extra. It is a voluntary programme for which they need to sign up, along with the manager. That gives the manager a lever to play a coaching and nurturing role. If the person qualifies, the rating changes retrospectively. They have seen 68% of the people in the enhancement pool sign up for the programme. And every month, there is a 10% to 15% increase in the upside of the productivity aspirations.

The officers in the 'valued performance' category are provided with opportunities to undergo training and skilling programmes. The bank has tied up with online universities for differentiated certification programmes. They are making it development-centric, and it is called the ACElerate (Axis Capability Enhancement) Programme.

The idea of performance management is to make it more positive and inclusive. Whether there is a system, or whether the bank moves away from rankings and ratings, the key challenge will be to manage differentiation. The journey for Axis Bank has not been easy, Ms Vempati agreed. But once it got established, it got expedited. "One of the conversations we keep having with people is the entire concept of feedback," she said, adding that if managers care for their employees, they will get more candid feedback. That element of care needs to be demonstrated.

(L-R) ***Ms. Jyoti Vij****, Deputy Secretary General, FICCI,* ***Mr. Ashwani Kumar****, Chairman, IBA and CMD, Dena Bank*
Mr. R Gandhi*, Deputy Governor, Reserve Bank of India.,* ***Mr. Bharat Poddar****, Partner and Director, BCG India.*

Valedictory Session

Valedictory Address: Mr R Gandhi, Deputy Governor, Reserve Bank of India

Mr Gandhi began his Valedictory Address with a 1994 quote from Bill Gates, then Chairman of Microsoft Corporation: "Banking is necessary, but banks are not." This was the theme of his address.

He pointed out that it takes time to discern the trends in any sector; unless the industry pauses to take a careful look, "emerging patterns are easy to be missed, at great cost to many stakeholders." He quoted from a number of published reports about the banking industry.

The July 2014 PWC Report on 'The Future Shape of Banking – Time for Reformation of Banking and Banks?' identified five global megatrends whose impacts, intersections and collisions were re-shaping the business of banking. The most influential of the trends were demographic and social change; new customer demands and stakeholder expectations; and technological breakthroughs that impacted everything from customer relationships to business models.

According to a Willis' research report published in Resilience in April 2015, the financial institutions industry, including banks, asset managers and financial technology companies, is facing a paradigm shift caused by a number of key megatrends. These trends were identified as regulatory capital requirements; digitalisation and technological advantages; new market participants; and demographic and behavioural changes in the new generation of customers. Another report by Scope Ratings in June 2016, titled 'Connecting the Dots of the New Paradigm Shift in Banking: Where Are We Now?' cautioned that the crossroads for banks at the intersection of technology, regulations and macro developments seem rather precarious.

What is common in all these reports, observed Mr Gandhi, is the recognition that emerging trends in technology, regulatory changes and consumer behaviour and expectations are redefining the role of banks, and even endangering their existence. If the banks do not pay heed to these developments, they risk emerging from the financial crisis "recapitalised, restructured, reformed, but irrelevant," he said, quoting from the reports. He focused on each of the three trends.

- **Technology**

Technological developments are changing the way banks and their customers interact. New entrants are seizing the opportunity to disrupt traditional business models and penetrate new markets. Fintech companies are emerging and using the technology to offer lower cost services such as e-payments and online trading. Social media companies such as Facebook, Twitter and Google have a huge customer following and are entering into the financial sector, bringing new sources of competition.

- **Consumers**

There is a new generation of young people known as 'millenials'. Their expectations and ways of interacting with banks are different. They do not like to visit banks, but instead prefer to avail of the services through online and social media-based platforms. On the other hand, mature, older and retired customers are demanding improved returns from investments and greater transparency.

- **Regulation**

Ever since the financial crisis, regulatory emphasis has been on capital. This has led many banks to divest themselves of risky, capital-intensive assets, businesses and even markets. It has resulted in a change in bankers' attitudes towards risk; and clearly demarcated the boundary between retail and wholesale banking. The strict enforcement of regulations paved the way for the growth of non-banking financial institutions; these are shadow banks, not subjected to the same degree of intense regulation as banks. They offer competing services to the clients of the banks.

These three trends have redefined banking and banks. Mr Gandhi considered whether they are actually endangering the existence of banks. "From the time the concept of money was understood, the concepts of lending and borrowing came into existence," he noted, adding that at that stage there was no concept of banking. The prototypes of modern banks were established about 700 years ago when organised lending and borrowing took place. Banks also took on remittance as a service. These services of borrowing, lending and remitting, came to be known as 'banking'.

Describing how the new megatrends have redefined banking, Mr Gandhi said, "Actually it is not redefinition in my opinion, but de-definition. Banking is no longer what a bank does. It is also what a non-bank does." The norm is now 'chunking' in banking. Technology and customer expectations have 'chunked' away the different elements of banking. There are some specialised entities who undertake only those chunks, such as P2P and P2B services. These entities have gradually chipped away chunk after chunk of banking. These non-banks now have enormous opportunities for growth. As Mr Gandhi put it, "With their specialisation and focussed service rendering, they are able to offer that chosen service at greater efficiency, speed, and at very affordable cost to the consumers."

"Is there an element of banking that remains the exclusive privilege of banks? Sadly, no," Mr Gandhi regretted. It is a moot point whether banks will really cease to exist. He quoted from a research report: "While we are not looking at the end of banking, we are surely looking at the end of banking and banks as we currently know them."

Unconventional policies are rampant all over the world. First, it was low interest; then near zero interest; then zero interest. Now there are negative interests. "Jurisdiction after jurisdiction is ushering in a negative interest rate regime." And there is no lower limit for that. The justification for banks to exist is a serious question. Why, Mr Gandhi asked, should society accord them the special privilege of banking and prohibit others from entering the business? In fact, he pointed out, "the West no longer officially designates anybody as a bank; they have only a depository institution or a credit institution."

Another challenge for the existence of banks is society's reaction to the financial crisis. With decreased consumer trust, financial institutions are acknowledging the need for new perspectives and paradigms in the services they offer. The effect of regulatory requirements on capital and market pressures on banks to leverage capital also greatly impacts the existence of banks. Mr Gandhi explained: "If we add the capital requirement as per TLAC prescriptions, bankers' usual cautionary additional capital, yet another add-on as per the public expectation as a fallout of stress tests assessments, I am afraid banks will end up with a debt equity ratio of about 4:1, which is not too different from highly levered corporates. That's one of the reasons why we are very cautious and hesitant about supporting TLAC whole hog."

Therefore, he said, the prognosis is that either banks will be dead, or at least the banks of the future will not be the banks of yesterday or today. He admitted that this sounded pessimistic. But, he informed the gathering, "we have to recognise the realities of the day, the compulsions of the new driving forces that demand a new paradigm in banking, and reflect on future course of action."

But the industry is not devoid of hope. First, it should take full advantage of the technological developments to meet customer expectations. "The new consumer is addicted to connectivity, convenience and freedom. They want not just value-added services, but such services anytime, anywhere, anyhow." Some researchers suggest that while banks may urgently need to embrace new information-based technologies and identify new avenues for growth, what is of paramount importance is for them not to lose sight of their social responsibility as financial service providers. Balancing profit with customer benefit must be at the heart of any new paradigm. Banks can play a much larger socially relevant role than any of the chunked entities in areas such as financial inclusion; green financing; anti-money laundering; countering financial terrorism; and even in anti-tax avoidance efforts.

Mincing no words, Mr Gandhi reminded the bankers present that there is still "one big area which you let others occupy by your lacklustre attitude, for you to rightfully reclaim, if only you make a concerted and conscious effort." That area, he specified, is SME financing. SMEs are a major, yet often overlooked sector by formal financial institutions. This is the case all over the world. They account for more than half of the world's GDP, and employ almost two thirds of the global work force. The International Financial Corporation reported that a 'funding gap' of more than $ 2 trillion exists for small businesses in emerging markets alone. In recent times, fintech companies have entered this space, with great success. This development can be a game changer for small businesses. "If only banks can change their current reluctant attitude towards SME financing, they can be a good antidote to these risks and display their socially relevant role," he declared. This can in turn justify their existence in the future.

Mr Gandhi ended his address with a word of advice to banks: "If you make yourself socially relevant, not just relevant in the economic sense alone, you can have hopes to exist."

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