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GIST OF YOJANA

JANUARY 2018

BANKING REFORMS

Shankar IAS Academy™

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I N D E X

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1. RURAL BANKING: TRANSLATING VISION TO REALITY

Why banks are hesitating to open branches in rural areas?

- Rural households have irregular income and expenditure patterns and hence banks will have high non performing loans in the rural areas.
- The loan waivers driven by political agenda and the economy behaving to the tunes of monsoon aggravate the problem further.
- The average ticket size of both a deposit transaction and a credit transaction in villages is small, which means banks need more customers per branch or channel to break even.
- Since many rural folks are not literate and so not comfortable using technology driven channels like ATMs, phone banking or internet banking, hence mostly dependent on bank branches, leading to banks' high cost to serve.
- The highly irregular and volatile income streams and unscheduled expenditure like medical and social emergency, attribute to higher risk of credit for the banks.

What are the steps to be taken to promote rural banking?

- For optimum usage of Banking Correspondents they need to be adequately compensated by banks so that they are sufficiently incentivised to provide banking services to villagers at their door steps.
- Banks need to initiate suitable training and skill development programmes to the BCs for their effective functioning.
- To wean away villagers from borrowing from money lenders, banks should develop simplified credit disbursement procedures and also flexibility in their processes.
- To reduce the overall transaction ticket costs in rural areas, use of domestic Rupay cards must be promoted in large scale.
- Since remittance facility for migrant population is of paramount importance, providing easy and cheap remittance facilities to migrants is an absolute imperative.
- To deal with poor villagers, banks need to initiate training programmes to equip their staff as well as BCs on human side of banking.
- To achieve meaningful financial inclusion, banks should give priority for small farmers as compared to large farmers while sanctioning credit.
- There is a need to promote Electronic Benefit Transfer systems effectively for boosting rural banking.
- Govt banks should initiate steps to increase the credit absorption capacity in rural areas by promoting employment and other opportunities.

- The need for vernacularisation of all banking forms is an absolute must, at least in major languages.
- As a part of financial literacy drive, bans need to take proactive steps in helping the common public to get over their English phobia.

What are the challenges encountered by Banking system due to new initiatives?

- A large number of PMJDY accounts do not have any money and lie dormant which only increases costs of banks to run these accounts.
- Poor people live on subsistence level of earning and with no source of regular earning, they don't have surplus to save in bank account or take any other financial instrument.
- Payment banks will have the benefit of wider reach but they will need to counter the issues of complex user interfaces, lack of internet penetration and lack of grievance redressal mechanism which might deter users.
- Direct benefit transfer may see collaboration of erstwhile middle men with bank officials to delay/deny benefits.
- Payment banks might also deprive regular banks of the fee income they earn from customers like those of making demand drafts, cash transfers, remittances, cash withdrawal through cheques and ATM transaction fees.
- In quite number of cases, the Business Correspondents have been accused of siphoning the money.
- Banking technology related frauds are increasing at the alarming rate.
- In rural and hinterland areas mobile connectivity is still in poor condition.
- Even some villages need the electrical connection also which is essential for the new age services of banking.
- Schemes like PMJJBY, PMSBY, APY etc are largely dependent on the success of banking reaching the poor and face a herculean task when a large section of population does not have access to or awareness of pension or insurance products.

2. STRENGTHENING OF CYBER SECURITY

What are the measures to be taken to ensure secure financial transactions?

- The originator of any transaction shall ensure that his device from which he is originating is completely cyber sanitised. The devise should have been patched up with latest Anti Virus signatures.
- Care should have been taken to type the banking website addresses and if it is an online transaction it should not be clicked from an email as it can route to phishing attacks.
- "No lunch is free lunch" - Any mobile / online tools which are offered free or given free should be dealt or used with due diligence.
- The PIN which is used by the originator should be kept confidential and should not be shared with anyone or through any link.
- The financial institution act as an mediator in transaction between an

originator and the beneficiary, so the financial institution IT systems must be protected well enough to carry out the safe and secure transaction.

- Data must not be changes during the transit, and steps must be taken to ensure that data cannot be altered in an unauthorised manner.
- The IT infrastructure of the financial institutions which are interacting online must conform to the standards and procedures created by the nodal agencies like CERT - In.

What are the steps taken by GOI to promote cyber security?

- In order to address the issues of cyber security in a holistic manner, the Government has released the "National Cyber Security Policy-2013" for public use and implementation by all relevant stakeholders.
- Government has setup National Critical Information Infrastructure Protection Centre (NCIIPC) to protect the critical information infrastructure in the country.
- Action has been initiated to set up a centre for tracking all the compromised systems connected on the Internet in the country and clean them on online basis so that the infection does not carry forward.
- All government websites are to be hosted on infrastructure of National Informatics Centre (NIC), ERNET India or any other secure infrastructure service provider in the country.
- All the new government websites and applications are to be audited with respect to cyber security prior to their hosting. CERT-In provides necessary expertise to audit IT infrastructure of critical and other ICT sectors.
- Indian Computer Emergency Response (CERT-In) has empanelled a total no. of 45 security auditors to carry out security audit of the IT infrastructure of Government, Public and Private sector organizations.
- All the Ministries/ Departments of Central Government and State Governments have been asked to implement the Crisis Management Plan (CMP) to counter cyber attacks and cyber terrorism.
- The National Watch and Alert System - Indian Computer Emergency Response (CERT-In) team is working 24/7 and scanning the cyber space in the country. The team works with Government, Service Providers, private sector and citizens both on pro-active and reactive basis and help in mitigating cyber incidents.
- Cyber Security mock drills are being regularly conducted to prepare the organizations to detect, mitigate and prevent cyber incidence.
- Sectoral CERTs have been functioning in the areas of Defence and Finance for catering to critical domains. They are equipped to handle and respond to domain specific threats emerging from the cyber systems.

List out some recent initiatives?

- **USB Pratirodh** - A desktop security solution, which protects from USB mass storage device threats.
- **AppSamvid** - A desktop solution which protects systems by allowing installation of genuine applications through white listing. This helps in preventing threats from malicious applications.
- **M-Kavach** – An indigenously developed solution to address the security threats in mobiles.
- **Browser JSGuard** - An browser that detects and defends from malicious HTML & JavaScript based attacks made through the web browser. It blocks access to the harmful, inappropriate and dangerous websites that may contain malicious content through Heuristics.

3. MISSION INDRADHANUSH : REVAMPING OF PUBLIC SECTOR BANKING IN INDIA

What are the reasons behind the need of banking reforms?

- The Public Sector Banks (PSBs) play a vital role in India's economy.
- In the past few years, because of a variety of legacy issues including the delay caused in various approvals as well as land acquisition etc., and also because of low global and domestic demand, many large projects have stalled.
- Public Sector Banks which have got predominant share of infrastructure financing have been sorely affected.
- It has resulted in lower profitability for PSBs, mainly due to provisioning for the restructured projects as well as for gross NPAs.

What is mission Indradhanush?

- The GOI rolled out many reforms which are nicknamed as ABCDEFG reforms to revamp the banking sector and put the PSBs back on track and the reforms are as follows.

Appointments:

- The Government decided to separate the post of Chairman and Managing Director by prescribing that in the subsequent vacancies to be filled up the CEO will get the designation of MD & CEO and there would be another person who would be appointed as non-Executive Chairman of PSBs.
- This approach is based on global best practices and as per the guidelines in the Companies Act to ensure appropriate checks and balances.
- The selection process for both these positions has been transparent and meritocratic and even private persons were allowed to apply for these posts.

Bank Board Bureau:

- The BBB will be a body of eminent professionals and officials, which will replace the Appointments Board for appointment of Whole-time Directors as well as non-Executive Chairman of PSBs.
- They will also constantly engage with the Board of Directors of all the PSBs to formulate appropriate strategies for their growth and development.

Capitalization:

- As of now, the PSBs are adequately capitalized and meeting all the Basel III and RBI norms.
- However, the Government of India wants to adequately capitalize all the banks to keep a safe buffer over and above the minimum norms of Basel III.
- So the estimated capital requirement of extra capital for the next four years up to FY 2019 is likely to be about Rs.1,80,000 crores and it will be infused to the banks in proper time intervals.

De-stressing PSBs:

- The infrastructure sector and core sector have been the major recipient of PSBs' funding during the past decades.
- But due to several factors, projects are increasingly stalled/stressed thus leading to NPA burden on banks.
- So initiatives like Creation of Project Monitoring groups in respective Ministries, facilitating faster policy decisions, programmes to de stress the DISCOMs are taken to improve the condition of PSBs.

Empowerment:

- The Government has issued a circular that there will be no interference from Government and Banks are encouraged to take their decision independently keeping the commercial interest of the organization in mind.
- A cleaner distinction between interference and intervention has been made.
- With autonomy comes accountability, accordingly Banks have been asked to build robust Grievances Redressal Mechanism for customers as well as staff so that concerns of the affected are addressed effectively in time bound manner.

Framework of Accountability:

- A new framework of Key Performance Indicators (KPIs) to be measured for performance of PSBs is being announced.
- Operating performance evaluated through the KPI framework will be linked to the performance bonus to be paid to the MD & CEOs of banks by the Government.
- The quantum of performance bonus is also proposed to be revised shortly to make it more attractive.

Governance Reforms:

- The process of governance reforms started with "Gyan Sangam" - a conclave of PSBs and FIs organized at the beginning of 2015 in Pune which was attended by all stake-holders including Prime Minister, Finance Minister, MoS (Finance), Governor, RBI and CMDs of all PSBs and FIs.
- There was focus group discussion on six different topics which resulted in specific decisions on optimizing capital, digitizing processes, strengthening risk management, improving managerial performance and financial inclusion.
- The Government has been constantly engaging with the Banks through review meeting and sessions for

strategic reviews etc to ease the Governance process.

What are the game changing initiatives taken by GOI in last one year?

- **Insolvency and Bankruptcy Code** : The objective of the new code is to promote entrepreneurship, availability of credit, and balance the interests of all stakeholders by consolidating and amending the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner and for maximization of value of assets of such persons and matters connected therewith or incidental thereto.
- The code aims to consolidate the laws relating to insolvency of companies and limited liability entities (including limited liability partnerships and other entities with limited liability), unlimited liability partnerships and individuals, presently contained in a number of legislations, into a single legislation.
- Such consolidation will provide for a greater clarity in law and facilitate the application of consistent and coherent provisions to different stakeholders affected by business failure or inability to pay debt.
- **Recapitalization of Banks**: The Government infused a sum of Rs. 25000 crore in 19 PSBs during financial year 2015-16 and Rs. 24997.182 crore into 16 PSBs during the FY 2016-17.
- Government has also allowed all PSBs to raise capital from Public markets through Follow-on Public Offer (FPO) or Qualified Institutional Placement (QIP) by diluting Government of India holding upto 52% in phased manner based on their capital requirement, their stock performance, liquidity, market conditions etc.
- **Consolidation of Banks** : The Union Cabinet has approved the framework for merging state-owned banks. Plans are to consolidate a total of 21 public sector banks.
- The motive behind the decision is to modify public sector banks according to suit the credit needs of the growing economy that is India.
- Also, the entities formed after merging PSU banks will be able to absorb shocks and can generate capital without depending on the state exchequer.

4. FACILITATING FINANCIAL INCLUSION

What is financial inclusion?

- Financial inclusion is a process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups in a particular at an affordable cost, in a fair and transparent manner.

What are the issues in financial inclusion?

- There is a need to extend the financial inclusion to the disabled, including those elderly with loco motor activity, vision and hearing is impaired.
- Even the RBI issued guidelines to make the banks to be disabled friendly, more steps are needed in this

direction to make more braches disabled friendly.

- Technological issues like frequent machine breakdowns and lack of connectivity which negatively impacts confidence of customers towards informal banking.
- There is an need for facilities lie biometric enabled and multi lingual hand held devices which can provide confidence in rural masses.
- To monitor developments regarding financial inclusion there is a need to assign responsibility to a dedicated financial institution.
- Financial literacy is a constant challenge and bankers have to adopt different strategies to reach the larger segments of the society.
- There is a need to standardise literature / material to extend financial literacy amongst the unbanked.

What are the initiatives of Government to enhance Financial Inclusion?

- **Pradhan Mantri Jan Dhan Yojana (PMJDY)** : Under this, a person not having a savings account can open an account without the requirement of any minimum balance and, in case they self-certify that they do not have any of the officially valid documents required for opening a savings account, they may open a small account.
- PMJDY offers unbanked persons easy access to banking services and awareness about financial products through financial literacy programmes.
- In addition, they receive a RuPay debit card, with inbuilt accident insurance cover of Rs. 1 lakh, and access to overdraft facility upon satisfactory operation of account or credit history of six months.
- **Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY)** : The PMJJBY is available to people in the age group of 18 to 50 years having a bank account who give their consent to join / enable auto-debit. Aadhar is the primary KYC for the bank account.
- The life cover of Rs. 2 lakh is for the one year period stretching from 1st June to 31st May and is renewable.
- Risk coverage under this scheme is for Rs. 2 lakh in case of death of the insured, due to any reason.
- The premium is Rs. 330 per annum which is to be auto-debited in one installment from the subscriber's bank account as per the option given by him on or before 31st May of each annual coverage period under the scheme.
- **Pradhan Mantri Suraksha Bima Yojana (PMSBY)** : The Scheme is available to people in the age group 18 to 70 years with a bank account who give their consent to join / enable auto-debit on or before 31st May for the coverage period 1st June to 31st May on an annual renewal basis.
- Aadhar would be the primary KYC for the bank account. The risk coverage under the scheme is Rs. 2 lakh for accidental death and full disability and Rs. 1 lakh for partial disability.

- The premium of Rs.12 per annum is to be deducted from the account holder's bank account through 'auto-debit' facility in one installment.
- **Atal Pension Yojana (APY)** : APY is open to all saving bank/post office saving bank account holders in the age group of 18 to 40 years and the contributions differ, based on pension amount chosen. Subscribers would receive the guaranteed minimum monthly pension of Rs. 1,000 or Rs. 2,000 or Rs. 3,000 or Rs. 4,000 or Rs. 5,000 at the age of 60 years.
- Under APY, the monthly pension would be available to the subscriber, and after him to his spouse and after their death, the pension corpus, as accumulated at age 60 of the subscriber, would be returned to the nominee of the subscriber.
- **Stand Up India Scheme** : The Scheme facilitates bank loans between Rs.10 lakh and Rs.1 crore to at least one Scheduled Caste/ Scheduled Tribe borrower and at least one Woman borrower per bank branch for setting up greenfield enterprises.
- This enterprise may be in manufacturing, services or the trading sector.
- The scheme which is being implemented through all Scheduled Commercial Banks is to benefit at least 2.5 lakh borrowers.
- **Pradhan Mantri Vaya Vandana Yojana** : As per the scheme, on payment of an initial lump sum amount ranging from a minimum purchase price of Rs. 1,50,000/- for a minimum pension of Rs 1,000/- per month to a maximum purchase price of Rs. 7, 50,000/- for maximum pension of Rs. 5,000/- per month, subscribers will get an assured pension based on a guaranteed rate of return of 8% per annum, payable monthly.

5. MANAGING NONPERFORMING ASSETS : A PARADIGM SHIFT

What are the reasons for the rise in Non Performing Assets?

- Exuberance in increasing balance sheet size by lending to borrowers unworthy of such loans on account of their past credit history.
- Funds were borrowed for creating excess capacities in anticipation of demand without factoring in the global capacities / demand position.
- Project completion was delayed for various reasons.
- Recovery of receivables was poor.
- The concerned corporate was not able to raise capital through the issue of equity or other debt instruments from capital markets and used borrowed money as equity leading to double leveraging.
- Business failure because of overestimated optimistic projections.
- Diversion of funds meant for expansion / modernization. Borrowed funds are not utilized for the purposes which they have borrowed.
- Willful defaults, siphoning of finds, frauds, misappropriation etc.,

- Lack of skill on the part of the banks to monitor end use of funds and diversion by the borrower through web of shell companies etc.,
- Deficiency in credit appraisal and improper due diligence.

What are the changes needed and reforms taken to contain NPA problem ?

- **Amendment in banking law to give RBI more powers** : The Banking Regulation Act may be amended to give RBI more powers to monitor bank accounts of big defaulters.
- The amendment in the banking law will enable setting up of a committee to oversee companies that have been the biggest defaulters of loans.
- RBI wants stricter rules for joint lenders' forum (JLF) and oversight committee (OC) to curb NPAs.
- **Stringent NPA recovery rules** : The government has over the years enacted and tweaked stringent rules to recover assets of defaulters.
- The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act or Sarfaesi Act of 2002 was amended in 2016 as it took banks years to recover the assets.
- Experts have pointed out that the NPA problem has to be tackled before the time a company starts defaulting.
- This needs a risk assessment by the lenders and red-flagging the early signs of a possible default.
- **RBI's loan restructuring schemes** : RBI has over the past few decades come up with a number of schemes such as corporate debt restructuring (CDR), formation of joint lenders' forum (JLF), flexible structuring for long-term project loans to infrastructure (or 5/25 Scheme), strategic debt restructuring (SDR) scheme and sustainable structuring of stressed assets (S4A) to check the menace of NPAs.