OCTOBER 2023

IBS VIGYAN

VISIONING BANKERS

Evangelistically Speaking

Dear Stakeholders,

RBI's principle based approach in engaging with regulated entities through "Supervisory Review" process under Pillar II of Basel Committee recommendations and the evolution of norms to nudge banks to move to expected credit loss computation process is covered in this month's Curated Cube. Another offshoot of the supervisory rigour has been the practice of imposing penalties on regulated entities by RBI. During this month, ICICI Bank has been fined ₹ 12 crores for extending loans to entities where the Bank's directors were involved and the bank failed to maintain the arm's length distance policy. Kotak Mahindra Bank has been fined ₹ 3.95 crores for failing to conduct review of entities engaged for outsourcing activities. Bank of Baroda has staked its reputation risk with RBI ordering the bank to suspend its "bob world" application. While the app has been found to be user friendly and well received, the order to suspend its rollout seems to carry other reasons. Bank of Baroda's management had been pushing its staff to increase the number of customers who have been onboarded to this app. Resultantly, driven by fear and ingenuity to achieve the numbers, many operating staff identified customers who have not been using any digital banking products. The staff populated their own mobile numbers in the customer master record and downloaded the app on their mobiles and started receiving OTPs too. Thus, the bank was on a roll in terms of the success of its "bob world" app rollout. As early instances of customers reporting loss of money from their accounts started pouring in, the bank's management began to panic. RBI has ordered the bank not to onboard any customers further, without RBI's permission. Maharashtra-based West End Housing Finance Ltd has been penalised for non-compliance with guidelines while taking over undertakings and breaching cap on holding management interest in the Co under different category of investors.

Moving over from monetary penalties, the JAIIB examinations of IIBF are under way. The CAIIB examinations will commence next week. The time when the preparations by the career aspirants reach frenzied heights. My humble exhortation to the candidates would be to not attempt any short cuts in collecting the aggregate minimum and stake their claim with their bank for monetary benefits. Instead, you must see this as a better opportunity to familiarise yourself with the macro level implications of regulatory guidelines.

Happy Saraswathi Pooja wishes.

Looking forward to a sustaining engagement with all.

Sincerely Yours

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Curated Cube

Reserve Bank of India (RBI) has been administering the Supervisory Review function envisaged under Pillar II of Basel III recommendations through the Internal Capital Adequacy Assessment Process (ICAAP) policy of the regulated entity as well as the adequacy of Provision Coverage Ratio. As against the rule-based approach of Pillar I, this is a principle-based approach. Aligning with international practices, Indian Banks have also been making graded provisions for loan losses after signs of delinquency have surfaced, i.e. after the account turns non-performing. At times, the degradation in asset quality has been faster than expected and enforceability of security interest becoming weaker day by day. Hence the need for shift from incurred loss-based provisioning to "expected loan-loss provisioning", to be aligned with emerging global practices.

Accordingly, RBI released a Discussion Paper on 16th January 2023 on this subject. Based on the feedback received, they have constituted an external working group to delineate the contents of the Discussion Paper. The External Working Group is headed by Shri R. Narayanaswamy, retired Professor, IIM, Bengaluru and has eight other members drawn from academia and practicing bankers.

The building of internal models for computing expected credit losses must satisfy, at minimum, certain parameters.

1. The model must satisfy the guidelines to be set out by RBI based on the guidance from IFRS 9 and principles laid out by Basel Committee on Banking Supervision (BCBS).

2. The model must be independently validated to ensure that it does not have any built-in bias, that could lead to underestimation of expected loan loss. It must also be put to back testing and internal validation.

3. The expected credit loss number thrown up by the model will be subject to a prudential floor to be prescribed by RBI based on comprehensive data analysis.

4. Banks will have to adhere to a non-exhaustive list of disclosures to be put out by RBI.

Considering the complexities involved in designing the models and the time required to test them, sufficient time shall be provided for implementation of the framework after issue of the final guidelines. Further, in order to enable a seamless transition, as permitted under the Basel guidelines, banks shall be provided an option to phase out the effect of increased provisions on Common Equity Tier I capital, over a maximum period of five years. This initiative could turn out to be another measure to strengthen the banking system in India.

(Cube gives a third dimension in geometry. Curated Cube endeavors to conflate events in the market over the past month.)

FOURTH PILLAR

OPERATION TWIST: It is monetary policy strategy of RBI. The objective is to stimulate economic growth of the country by lowering the long-term interest rates. Simultaneous purchase and sale of Govt. securities under Open Market Operation is carried out, which is known as Operation Twist. The operation involves purchasing of long tenor securities while selling short tenor securities to keep the yield curve under check and thereby lowering the borrowing cost.

CONVERSATIONAL PAYMENTS IN UPI: Artificial Intelligence (AI) is becoming increasingly integrated into the digital economy. To enhance the ease of use and convenience, conversational instructions will be much beneficial to users. Therefore, RBI has proposed to launch an innovative payment mode namely "Conversational Payments" on UPI, that will enable users to engage in a conversation with an AI-powered system to initiate and complete transactions in a safe and secure environment.

UDGAM–UNCLAIMED DEPOSITS– GATEWAY TO ACCESS INFORMATION: This is a centralised web portal developed by RBI, for use by members of public to facilitate and make it easier for them to search their unclaimed deposits across multiple banks at one place. The user can identify and then can either proceed to claim the amount or make the deposit account operative at their respective banks.

REQUIREMENT OF MAINTAINING ADDITIONAL CASH RESERVE RATIO: U/s 42 (1) of RBI Act 1934, an additional average daily CRR balance over and above the prescribed CRR is required to be maintained by all SCBs w.e.f. 12.08.2023. The amount of such additional average daily balance of CRR should not be less than 10% of the increase in NDTL between 19.05.2023 to 28.07.2023.

LAKHPATI DIDI SCHEME: The scheme is aimed to provide skill training to two crore women across the nation. The 'Lakhpati Didi' scheme is designed to empower women by equipping them with essential skills that pave the way for the establishment of micro-enterprises.

(Fourth Pillar strives to position beyond the three pillars of Basel and is culled from the Four Estates)

INQUISITIVELY SPEAKING

1. With the objective of the development of the Corporate bond market from the perspective of Mutual Funds, SEBI has allowed Asset Management Companies to participate in __ on Commercial Papers (CPs) and Certificate of Deposits (CDs).
a) Reverse Repo
b) Term Money
c) Repos
d) Call Money

2. An IDF-NBFC means a non-deposit taking NBFC which is permitted to (i) refinance post commencement operations date (COD) infrastructure projects that have completed at least ______ of satisfactory commercial operations; and (ii) finance toll operate transfer (TOT) projects as the direct lender.
a) One year
b) Two years
c) Three years
d) Four years

3. Net Owned Fund (NOF) and Regulatory capital (CRAR) of an IDF-NBFC to be at least, ___ Crore & ___% respectively.
a) 200, 10%
b)300, 15%
c)400, 12%
d)500, 15%

4. To encourage wider adoption of small value digital payments in offline mode, RBI has proposed to increase the existing limit of ₹200 per transaction with the overall limit of ₹2000 per payment instrument to ₹_____ per transaction.
a)250 b)300 c)350 d)500

5. Legal Entity Identifier (LEI) is applicable for large corporate borrowers having exposure ₹ __ crore and above as on 30th April 2023.
a) 25 b) 50 c) 75 d) 100

6. For a borrower to be declared Wilful defaulter, the cut off limit is ₹__ lakh or more:
a) 10 b) 25 c) 50 d) 100

ANSWER KEY

1.c 2.b 3.b 4.d 5.a 6.b

Stretch n Speak

FBIL: Financial Benchmarks India Private Limited.

IDF-NBFC: Infrastructure Development Fund – Non-Banking Financial Company.

DPDPA 2023: Digital Personal Data Protection Act 2023.

CSIS: Central Sector Subsidy Scheme.

PFCE: Private Final Consumption Expenditure.