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The two facets of NPA management

Santosh Kumar Das & Divya Sharma

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THE HINDU

The phenomenal increase in non-performing assets (NPAs) and wilful defaults over the last three years raises serious concerns about the effectiveness of NPA management and its mechanisms. Given the potential adverse impact that the increasing incidence of NPAs might cause, it is critical that NPA resolution takes place in a timely manner. Policies concerning NPA resolution must address two critical aspects: first, how to prevent it occurring at this scale in the future? and second, how to manage the existing accumulated NPAs?

Till recently, most of the initiatives by the government and the RBI (Reserve Bank of India) had centred on the latter — how to manage the existing NPAs. The emphasis was on finding ways to reduce the magnitude of NPAs. This was driven by the idea that bank balance sheets must be cleaned up and restored. While it is important to clean up the balance sheet of banks by reducing or eliminating bad loans, it is equally important to think about preventive measures. Typically, preventive measures are structural in nature. Both elements are quite important to a robust NPA management mechanism.

Regulator's role

The government and the regulator have to play a greater role in the process of NPA management. The role of the government has historically been crucial when there is a banking failure or crisis. It is the government which comes to the rescue, either through direct intervention or through the regulator. The role of government becomes even more important as it happens to be the principal owner of the majority of the affected banks in India.

On preventive measures, there is a need for evolving a framework in order to bring transparency into the operation and management of SCBs (scheduled commercial banks), particularly the PSBs (public sector banks), on four major parameters — project appraisal, monitoring, accounting, and auditing. As large loans constitute a substantial portion of the total NPAs, a robust credit appraisal mechanism is very much required. As large loans tend to be relatively technically complex, the banks must enhance their technical capabilities to undertake project monitoring effectively. Greater emphasis must be placed on bringing efficiency and transparency into the accounting system. Emphasis should be given on strengthening the audit system in banks.

The above measures can potentially reduce the possibilities of collusion among the officials of the funding institutions and the borrowers.

'Bad bank'

On NPA resolution, to deal with the existing accumulated NPAs, there is a need for creating a publicly funded 'bad bank' or an asset management company which will deal with the stressed assets of PSBs. The approach should be to formulate a resolution mechanism which will maximise recovery, and thereby, reduce the burden on the banks or the government. It can be very similar to the Swedish model where the bad bank bought the stressed assets from the affected banks and sold it at a higher price at the time of economic expansion, when asset prices picked up. This way, recovery on the bad loans can be maximised. The life span of the Swedish bad bank 'Securum' was 15 years, and it was fully owned by the government.

On a similar line, the Government of India, too, can create a bad bank, with full government ownership. The proposed institution can continue to exist without an expiry date as the NPA problem is perennial.

The managerial staff of the 'bad bank' may, however, be outsourced to boost operational and managerial efficiency.

The proposed bank should function independently with greater professionalism and should be accountable to the government.

Given the fiscal constraints, it may not be viable for the government to finance the proposed bad bank through budgetary support fully. The government can, however, partly finance the proposed 'bad bank' by issuing equity shares with the government holding the majority share.

Small farmers can be growth engines, not just beneficiaries: Rodger Voorhies

India has a long way to go in formulating policies for the uplift of small and marginal as well as landless farmers, says Rodger Voorhies of Bill and Melinda Gates Foundation

Jun 25 2018 | Elizabeth Roche, THE MINT

New Delhi: India has made much headway in tackling its open defecation and sanitation problems but still has a long way to go in formulating policies for the uplift of small and marginal as well as landless farmers, says Rodger Voorhies, executive director of the agricultural development, financial services, gender equality and water, sanitation and hygiene programmes at the Bill and Melinda Gates Foundation. Smallholder farmers need to be seen as an engine of economic growth, not just a beneficiary, said Voorhies who was on a visit to India last week. Edited excerpts from an interview:

The issues that you look after in the Bill and Melinda Gates Foundation—sanitation, women's empowerment, women's inclusion, financial inclusion, etc. are priority programmes of the Indian government. How far do you think we have come in the past four years?

I think it depends on the area you focus upon. If you look in the area of sanitation, the Prime Minister has made “Swachh Bharat” such a focus. It’s not just a focus on building toilets. The mission has evolved to how do we eliminate open defecation and safely manage and treat human waste. We think there has been a lot of progress. We are seeing the right policies being put in place that have a long-term effect. We’re seeing the building up of local organizations who are creative and entrepreneurial on the ground to solve this. And we’re seeing a long-term resolve from the government to know that this is not something that will happen overnight. So, in that area, we feel like there’s great progress being made.

In the area of digital financial inclusion, I have all the hope in the world that India may lead the world in what an inclusive financial system of the world can look like. And when I look at the numbers going through the Unified Payment Interface, they are growing by millions every day, we are seeing hundreds of millions of people being brought into the financial system in a way they haven’t been before, and I think the question that remains for us is are we seeing the results of that in poverty impact and resilience, and I think it’s too early to tell yet, although there is some good information on how even small changes in access have poverty impact. The one area I would like to see the government move forward is in the area of smallholder farmers, and actually moving beyond the food security agenda, and into how do we really operationalize this doubling of incomes, how do we see smallholder farmers as an engine of economic growth and not just a beneficiary. I feel like we’re in the beginning stages of that and I’m hoping that continues.

It’s interesting that you mention doubling farmer incomes because in India, we have two problems. First of all, small holdings, and secondly, you do have a population of landless farmers. So how realistic is this ambition of doubling farmer incomes by 2022?

Farmer incomes are already low so I’m less worried about doubling the number than what is a long-term sustainable system. If you look at the history of agri transformation, if you look at countries like China, Vietnam, Cambodia—one of the things that stood out is they saw their smallholder farmers going through stages of market development. The first stage let us generate surplus and then let us move into diversification, and then from that, you have this process of both initial labour absorption, greater productivity and then you have off-taking of that labour to other parts of the market. And so the key ingredients of that have been good extension, good market connectedness, flexibility in land rents so that people can actually consolidate land and rent it out in a safe way. And I'm not sure if we've seen all those policies put in place. So, I am worried about the landless issue, but I do think if there is a sizable population of smallholding, if we have the right policies in place we would see that productivity gain, and then we see the market forces start to take over, including export markets. So, I believe the landless issue is a real challenge and the government of India is looking into it, but I do believe, let's start with the tens of millions of farmers who do have small holdings, get their productivity up, and then work on the landless issue. We are at the beginning stages but we need to put in place incentives that allow the flexibility of the market, because they're not the same ones that led to the green revolution.

You mention that women contribute 17% to India's GDP. What steps can bring more women into the workforce?

I think it's a complex problem with social and economic dimensions, and I think part of this will happen as programmes (for women) roll out. I don't think there's going to be this cookie cutter image of it worked in Bangladesh so it should work in India or it worked in Africa so it should work in India. And so I think we're going to have to ask ourselves a set of questions. What are the meaningful policies that bring women into the economy? Time poverty is a real issue—issues of family leave, crèche, these seem to make a big difference. I think the next question is—what is the infrastructure women need to fully participate or pursue higher levels of secondary education completion. We're seeing higher levels of tertiary and primary education. But then, there is this big falloff where women aren't getting the jobs right after, and why is that? I think there is probably both an economic and a social dimension and I think that's where we are going to have to work with local organizations, including self help groups (SHGs)—a social infrastructure created by the government of India covering nearly 50-70 million women, to understand where that disconnect is and what's the collection of benefits that will help improving women's access to work, incomes, and social leadership roles. What we do know from the world is that when the right policies are put in place, when the right evolution of social norms and benefits get put in place, women do respond to those economic incentives.

One of the things this government takes credit for is digital financial inclusion, Aadhaar and bank accounts. There have been reports that these systems create more exclusionary tendencies in terms of verification processes—they are troublesome, difficult. Do you think the Aadhaar system is actually not as inclusive as it should be?

I actually don't think I'm in a position to judge where Aadhaar stands, but globally there are a few things that stand out. One is that low-income people suffer from being under-known and that makes it really hard for them to fully participate in the economy and that shows up in three ways. I don't have or can't afford access to all the verification needed again and again for Know Your Customer or approve my ID again and again. And that's a frictional and expensive thing for low-income people to do. Secondly, if I don't have a way to be known or ID-ed, I often get taken advantage of; I don't get the benefits I am supposed to from government. I don't feel empowered to give my voice even if I'm questioning something. We have seen again and again that in countries that have a good ID system, it improves the empowerment of low-income people, it improves their economic participation and it lowers the cost of participation. So, they access healthcare better, they access financial services better. I think a programme that is low cost, robust and allows low-income people to have an ID is a good thing. Now, how Aadhaar works is something the Gates foundation doesn't have a view on. The last thing I'd say on that is, there are a lot of movements that said, we will build one system for wealthier or middle class people, and the poor people will have a secondary system—a different financial system, healthcare system, agri system. And I think any system that's inclusive, which brings everybody is the right way to go. An ID is a big piece of that because we think everybody benefits from an economy that includes everyone.

What do you see as challenges for India in the areas you mentioned?

If we look at the overall development goals, while India has made great progress, there is still a really large percentage of the world's low-income folks who live in India. And so, it's going to be how we continue the pace of growth that reaches these low income folks. And as we go deeper and deeper into the poverty pyramid, it becomes harder to do it. That's going to be a challenge.

A secondary challenge is, as the economy matures and grows, dealing with smallholder farmers is going to be an essential piece of growth, and I'm not sure we have figured out how we drive that productivity gain in India. And it's one that we at Gates Foundation are happy to partner India with, to explore how we can see how we can be helpful with our global experience. And I think nutrition is going to continue to be a big one because stuntedness is such a problem.

I think that's where we know some things work and we have to figure out how to roll those out to rural areas.

Upgrade software at ATMs by June 2019 or face penalty, RBI tells banks

SPECIAL CORRESPONDENT MUMBAI, JUNE 21, 2018

THE HINDU

'Use of unsupported version of operating system could affect customer interests'

With banks failing to upgrade software in automated teller machines (ATM) despite repeated reminders, the Reserve Bank of India (RBI) has now directed the banks to complete the process in a phased manner latest by June 2019.

'Slow progress'

"The slow progress on the part of the banks in addressing these issues has been viewed seriously by the RBI," the central bank said in a notification to banks.

The banking regulator pointed out that many ATMs were still running on Windows XP and other unsupported software. RBI had asked banks to upgrade the ATMs first in March last year and then in November. According to banking industry sources, there could be 30% of the present 2.2 lakh ATMs that still use old software.

RBI said the vulnerability arising from the ATMs operating on unsupported version of operating system and non-implementation of other security measures, could potentially affect the interests of customers and the banks' image.

Banks have been asked to upgrade 25% of the ATMs by September 2018, 50% by December 2018, 75% by March 2019 and all by June 2019. Security measures should be implemented by August 2018 and anti-skimming and white-listing solutions by March 2019.

RBI warned banks of penalty if they failed to adhere to the deadline. "It may be noted that any deficiency in timely and effective compliance with the instructions contained in this circular may invite appropriate supervisory enforcement action under applicable provisions of the Banking Regulation Act, 1949 and/or Payment and Settlement Systems Act, 2007," RBI said.

Nirav Modi stayed in flat above jewellery store in London: report

PTI | LONDON, JUNE 24

BusinessLine

Indian billionaire Nirav Modi was living in a flat just above his jewellery store in the post Mayfair area of London while he was being hunted in India for an alleged money laundering case linked to over USD 2 billion, according to a media report today.

The 47-year-old diamantaire was able to travel in and out of Britain at least four times since his passport was cancelled by the Indian authorities in February.

During his stay in London, he was reportedly living in the heart of the city above his jewellery boutique called "Nirav Modi" on Old Bond Street, which was reportedly closed last week, The Sunday Times reported.

"Why are they always ending up in London? It's as if the UK is a safe haven," the newspaper quoted an Indian official as saying.

That Modi has been using Britain as a "safe haven" threatens to damage diplomatic ties between India and the UK and further scupper prospects of a post-Brexit trade deal, the report warned.

Modi and his uncle Mehul Choksi are accused of benefiting from a huge fraud against the Punjab National Bank, the country's second largest lender, to the tune of more than USD 2 billion.

Indian court has issued warrants for the arrest of Modi and Choksi.

On February 23, the Indian authorities revoked Modi's passport, contacting Interpol and the UK government soon after. But official records reveal Modi travelled from Heathrow Airport to Hong Kong on March 15, and from New York to Heathrow Airport on March 28.

Three days later, he flew from London to Paris. On June 12, Modi is thought to have boarded the Eurostar train from London to Brussels, the newspaper claims, adding that unconfirmed reports claim Modi has applied for asylum in the UK.

The UK Home Office and Border Force declined to discuss individual cases but said in a statement: "All passengers attempting to enter the UK are subject to checks by Border Force officers to identify people of concern."

"Border Force works with international partners to ensure the most up-to-date information is available."

In the UK, Nirav Modi's jewels have been made famous by British actress Kate Winslet sporting the diamonds at the Oscars in 2016. Also, his advertising campaigns have been fronted by the British model Rosie Huntington-Whiteley.

Did ICICI Bank inflate profits, breach NPA rules?

The latest whistleblower complaint has alleged ICICI Bank inflated profits by at least $1.3 billion over eight years by delaying provisioning for NPAs

Top ICICI Bank executives, including CEO Chanda Kochhar and executive director Vijay Chandok, wilfully breached rules to avoid classifying the loans as bad, alleges the whistleblower complaint

Jun 25 2018 | Anirudh LaskarVarun Sood

live mint

Mumbai: ICICI Bank Ltd has not satisfactorily answered two serious allegations made by a whistleblower—that the bank inflated profits by at least $1.3 billion over eight years by delaying provisioning for bad loans, and that top executives, including CEO Chanda Kochhar and executive director Vijay Chandok, wilfully breached rules to avoid classifying the loans as bad.

On Friday, the bank failed to fully address these issues in response to a *Mint* query, although it denied charges of incorrect accounting of interest income in 31 loan accounts; misrepresenting recovery amounts in non-performing assets as fees; and overvaluing securities for corporate loans.

"In certain accounts, transactions were observed that may have delayed the classification of the account as non-performing under Indian GAAP (generally accepted accounting principles) in earlier years… As mentioned earlier, all the above loans had been classified as non-performing and provided for as per applicable norms by 31 December 2017," ICICI Bank said in its response, a copy of which was sent to the exchanges.

However, the complaint by the whistleblower, an ICICI Bank employee, made on 20 March and 22 March to the Reserve Bank of India and the Securities and Exchange Board of India (Sebi), has alleged that the bank deliberately failed to set aside funds to cover 31 defaulting loan accounts between fiscal 2008 and March 2016, not fiscal 2017. The bank's clarification does not answer the whistleblower's charges as to why in a number of fiscal quarters between 2008 and 2016, the bank's management deliberately delayed provisioning for 31 loans.

The bank has allegedly inflated profits, primarily by underreporting the quantum of bad loans made to 31 companies, in which impairment was delayed by a quarter to even up to five years, according to the complaint.

In its detailed rebuttal on Friday, ICICI Bank admitted there were some delays in underreporting the quantum of bad loans made to 31 companies. In response to a fresh query sent by *Mint* on Saturday, ICICI Bank declined to elaborate further, stating that "we have nothing further to add on this matter at this point of time".

According to the whistleblower, the bank has managed to delay provisioning for NPAs arising out of loans worth at least $3 billion. Effectively, ICICI Bank would have reported losses in some quarters over the eight years, had the bank's management not deferred impairment of loans, claimed the whistleblower.

It is not known if this points to a systemic failure at the bank and if the bank is also investigating executives responsible. It hasn't clarified yet if it intimated Sebi about the internal probe as part of fair disclosure norms.

The whistleblower's allegation of partiality by the bank's top management in cases of certain loans is also quite serious.

"The bank's top management has often openly discussed the methods to be used or have been used to avoid impairment of loans... there have been several meetings held at the bank by the senior management to discuss the modus operandi of trying to save certain loan assets in other countries by funding a group company in India. The bank's discussions in such cases indicate the involvement of Chanda Kochhar in negotiations with the client," reads the whistleblower's letter. It adds that the bank has on several instances modified the internal auditor's observations to mask the fraud from the final audit report at the behest of the senior management.

ICICI Bank did not respond to this charge.

According to the whistleblower, at least three loans, including a $923 million loan made to Essar Global Ltd, a loan of similar amount made to Bhushan Steel Ltd and a $615.38 million loan to Essar Steel Ltd account for 84% of the $2.92 billion in loans made to 31 firms.

ICICI Bank, which is also listed on NYSE and governed by the US Securities and Exchange Commission, on Friday, dismissed this charge saying that its interim internal report found no "material impact" on the bank's financials, without clarifying the threshold amount that is defined as "material" by the bank. Although GAAP and FASB (accounting methods) do not precisely stipulate a threshold to define materiality, according to auditors and courts in the US, on the income statement, any transaction constituting 5% or more of the company's pre-tax profit, or 0.5% of sales revenue, is considered as material.

On a balance sheet, any entry of more than 0.3-0.5% of total assets, or more than 1% of total equity, is considered to be material.

Attorneys and accountants at the SEC have been investigating the whistleblower's allegations for months now. The 20 March complaint states that the bank had engaged in fraudulent activities between 2008 and 2016 to avoid reporting of impairment of loans.

ICICI Bank has not clarified whether the US SEC is conducting any probe based on the allegations made in the whistleblower emails.

SEC considers it an abuse of materiality judgement if it is done to keep stock prices artificially high, or inflate reported earnings or understate the actual value of the asset base.

ICICI Bank has said that further actions in the matter are being and will be taken as directed by the audit committee, without clarifying on whether this initiative is related to either an ongoing investigation and what the role of senior management was in this delay in classifying some of the loans as NPAs.

Is LIC playing white knight or Don Quixote?

KR SRIVATS BUSINESSLINE - NEW DELHI, JUNE 25

Experts rue likely use of policyholder funds to rescue ailing state-owned bank

It's the same script playing out yet again, but with a slight twist.

Insurance behemoth LIC is seen to have been nudged by the Centre to do the rescue act, though the official word is the boards of the respective entities will take a call.

The main difference this time around is that there is no disinvestment process at play; rather, LIC will unilaterally try to prevent the ailing public sector lender IDBI Bank from going under.

The proposed move is not going well with finance experts, who are accusing the Centre of using policyholder funds to rescue IDBI Bank.

In the past, only taxpayers' funds were used for bailouts, they pointed out.

"LIC=ATM", tweeted Sanjay Bakshi, a professor of finance at the Management Development Institute in Gurugram.

The big question is whether LIC has the expertise to run a bank if it gets a controlling interest in IDBI Bank, say industry watchers. The Central Government, which owns an 81 per cent stake in IDBI Bank, may look to bring its holding below 50 per cent. However, it is not divesting its stake to LIC. Instead, IDBI Bank will make a preferential allotment to LIC through fresh equity of shares.

With the LIC board giving its go-ahead, the action has clearly shifted to the insurance regulator IRDAI and capital markets regulator SEBI.

The current regulatory norms forbid insurers from holding more than a 15 per cent stake in a company. IRDAI blessing is a must beyond this level. Also, since IDBI Bank is a listed entity, LIC ought to make an open offer. However, since two state-controlled entities are at play, SEBI might exempt it, say banking industry observers.

PCA framework

Last month, the RBI had brought IDBI Bank under its prompt corrective action (PCA) framework due to high NPAs and negative RoAs.

For the just-ended March quarter, IDBI Bank had reported a net loss of Rs 5,662.76 crore, wider than the net loss of Rs 3,199.77 crore in the same quarter last year.

Gross NPA as of end March 2018 stood at Rs 55,588 crore (Rs 44,753 as of end March 2017)

AIBEA THIS DAY JUNE 26	
1926	Com. P K Menon, Founder General Secretary, AIBOA (date of birth).
1975	National Emergency in operation, bipartite discussions stalled. Attack on our trade union rights launched by Bankers.
1984	AIBEA Central Committee meets at Mumbai.

Central Office: PRABHAT NIVAS
Singapore Plaza, 164, Linghi Chetty Street, Chennai-600001
Phone: 2535 1522 Fax: 2535 8853, 4500 2191
e mail ~ chv.aibea@gmail.com
Web: www.aibea.in