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The three big problems in India's banking sector, according to the RBI

Nupur AnandJ
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QUARTZ

India's central bank has some big concerns about the sustainability of the country's banking system.

In its bi-annual Financial Stability Report (FSR), released on June 30, the Reserve Bank of India (RBI) warned that the sector is under severe stress, with mounting bad loans and an increase in bank fraud, among other issues. All this, the RBI says, could drag down India's economy.

"Weak investment demand, partly emanating from the twin balance sheet problem (a leveraged corporate sector alongside a stressed banking sector) is a major challenge," the report said.

Here are the key problems plaguing India's banking sector, according to the RBI:

Bad loans

At nearly Rs10 lakh crore, India's pile of bad loans is bigger than the gross domestic products of at least 137 countries. But so far, the RBI's attempts to reduce Non-Performing Assets (NPAs) in the banking sector have yielded little result.

The share of gross NPAs in India could inch up to 10.2% by March 2018, from 9.6% in March 2017, according to the FSR. In September 2016, gross NPAs were at 9.2%.

Currently, the worst-hit are the state-owned banks, which dominate the Indian banking system. In March 2017, the average bad loans of PSBs stood at 75% of their net worth. These bad loans are squeezing banks' profitability and capital positions, threatening the health of some of India's biggest banks.

In the report, the RBI cautioned that the situation could get worse with any unforseen stress in the economy.

Cyber threats

An estimated 95% of transactions in India are paid for in cash but with the growing penetration of computers and smartphones, and increasing access to the internet, Indians are taking to digital channels for their banking needs. Cybercrime is becoming a greater threat as a result.

The FSR labeled cyber-attacks as a high-risk zone for India's banking sector. The RBI classifies bank fraud as transactions involving any cheating, negligence, misappropriation of funds, or forged documents.

"Not only simple attacks using phishing, vishing and social engineering, but also increasingly audacious attacks by organised gangs with or without backing by state players have come to light," the RBI said.

The clamour to secure India's banking system increased following a massive data breach of 3.2 million debit and credit cards last year, one of the biggest attacks in the country. Another red flag was the recentglobal ransomware attack that affected the computer systems of governments and several companies in various countries, including India.

The RBI recommended that banks invest in preventive software and frequently assess the risks at hand, not just for in-house operations but also for the external vendors that the lenders employ.

Bank fraud

Another pressing concern for the banking regulator is the increased number of fraudulent transactions at Indian banks. What's adding to the concerns is that banks often seem reluctant to report these cases.

"Almost all corporate loan-related fraud cases get seasoned for two to three years as NPAs before they are reported as fraud," the RBI said in the report.

In the last five years, the volume of bank fraud has increased by 19.6% to 5,064 cases.

Over 90% Indian customers still prefer branch over online banking: Report

BY IANS | JUL 03, 2017

NEW DELHI: While the government has been pushing people to go online when it comes to banking, the branch still continues to dominate banking channels in India, with 94 per cent of retail banking customers having visited the branch/store at least once in the past 12 months, a new study revealed on Monday.

According to the 2017 Oracle J.D. Power India 'Retail Banking Study,' despite the impetus provided by demonetisation, digital banking is not yet a pervasive experience in India.

"Most banking relationships still begin and continue at the branch. However, there is great potential for banks to move more into the digital space. Only 51 per cent of retail banking customers have a reliable online banking experience with their main financial institution," said Gordon Shields, senior director, J.D. Power, a US-based global marketing information services firm.

The results was based on in-person interviews with 5,368 retail banking customers conducted between February and April 2017 across 14 states and included both private and public banks.

"In fact, overall customer satisfaction with banking in India is lagging significantly behind other key markets at 672 index points, compared to the industry average score reported in other J.D. Power studies in China (806), the USA (793) and Australia (748)," Shields added.

The study measured overall satisfaction in five factors: account activities (39 per cent); account information (18 per cent); facility (17 per cent); product offerings (14 per cent) and fees (12 per cent).

While overall customer satisfaction with mobile banking is markedly higher (693) than with In-Person Branch interaction (676), only 9 per cent of India retail banking customers use mobile banking for everyday transactions.

"Among the 48 per cent of customers who have yet to download a banking app, one-fourth state lack of security is a key reason for non-usage," Shields noted.

Nearly three-fourths (73 per cent) of customers believe their financial needs were not fully understood before they were offered new products, with only 7 per cent having had fees and pricing of products explained.

"As India embarks on its digitisation agenda, results on ground exhibit a contrary reality," said Kiran Kumar Kesavarapu, APAC leader, industry innovation advisors-financial services Oracle.

"We believe the issue lies in customer engagement models that Indian banks employ today and related security uncertainties when transacting online. This can be addressed easily and quickly," Kesavarapu added.

Private banks outperformed public banks and were rated higher in overall satisfaction (680) than public banks (666).

Private banking customers are more likely to recommend their bank to friends and relatives (89 per cent) than public banks (86 per cent).

Use of mobile banking and digital payments gaining ground

JUL 03, 2017
THE ECONOMIC TIMES

73% made a purchase with a mobile app that can be used at many different retailers.

A study finds use of mobile devices and other digital banking channels by consumers in India has risen after demonetisation.

Key findings about Indian consumers

***** 18% of the respondents use their primary bank's credit cards exclusively.

* 30% of payments are done with mobile apps compared to cash, cheque or credit/debit cards.

* 60% of respondents have used mobile devices this year to check account balance, view recent transactions, pay bills, transfer funds or other banking needs.
The figure was 39% in 2016 and 34% in 2015.

Over the last 30 days

1. 64% of banked individuals reported using their bank's mobile app
2. 84% paid a bill from their bank accounts

3. 79% transferred funds between accounts

4. 73% made a purchase with a mobile app that can be used at many different retailers

5. 64% paid individuals through a bank's app

6. 62% paid an individual through a payment service's app.

Source: FIS' third annual PACE report, which surveyed 1,000 banking consumers in India

GST rollout: Key changes to IT systems by banks ensures no hiccup

BY SALONI SHUKLA, ET BUREAU | JUL 03, 2017

THE ECONOMIC TIMES

MUMBAI: Business in banks may have been smooth since the Goods and Services Tax (GST) regime began two days back, but the banking and insurance activities of customers will begin to pinch as tax rates on these services have risen, said bankers.

Most large sized banks had made significant changes to their IT systems in anticipation of the nationwide rollout of GST on July 1 and there has been no hiccup in the past two days, even though they were not normal banking days with July 1 seeing marginal activity since banks were busy closing books for the first quarter.

But customers will have to pay more as banking services such as debit card, home loan processing fee, locker rentals, issuing of cheque books, cash handling charges and SMS alerts would attract higher taxes.

"We are one of the largest tax paying entities in the country, so we have made sure that we can do the filings in every single state. Go Live has happened, so we are live everywhere," said Jairam Sridharan, CFO of Axis Bank.

"The first tax payments will happen in the next one month, but all the billings have changed to the GST format and we haven't had any problem."

State Bank of India and Axis are among the five banks that have been allowed to take GST payments across the country. SBI too announced its GST-readiness and said that GST payments could be made online through internet banking and SBI debit cards, or by using its 25,000-plus branches.

"We are completely GST-ready, all systems have been integrated and tested and we haven't come across any issues so far," said Mrityunjay Mahapatra, DMD, SBI. "There are 40 internal applications which have been aligned with the GST guidelines. Transactions are happening successfully and we are seeing lot of them happening through internet banking. Several customers are also doing small value transactions to find whether the system is working or not."

Some of the bigger private and multinational banks started modifying their front-end IT systems at the end of last year while several state-run banks and smaller private banks had floated tenders recently inviting IT companies to make them GST-ready.

Recently, the Indian Banks Association had called for a meeting to check the preparedness for banks and found that they are more or less ready to face the new tax challenges.

While most banks claim GST readiness, consumers will have to shell out more for banking services, insurance premium payments and credit card bills under the new regime. "Due to increased rate of tax on banking services from 15% to 18%, GST will result in increased cost of services offered to customers," said Ravindra Marathe, CEO, Bank of Maharashtra.

"GST has a mechanism of reconciliation of output services and input services, and banks may get the credit of each eligible input service. Overall, the monetary impact may be negative initially, but complete transparency in transactions will show positive results for the banks and the economy in the long term."

Also, life and non-life premiums would involve an increase in taxes from 15% to 18%.

"Though insurance customers will have to pay a higher rate of GST at 18% compared to 15% service tax earlier, the overall impact should be positive, given the convenience and simplicity associated with a single tax regime," said Gopal Balachandran, chief financial officer, ICICI Lombard.

Bank of England staff to stage four-day strike in pay row

Unite members at the Bank of England are to walk out later this month as a pay dispute escalates, the union says

03 July 2017

sky NEWS

The Bank of England is on course to face its first strike action in over 50 years as a pay dispute threatens disruption.

The Unite union said its members were to walk out for four days from 31 July in protest at the imposition of a 1% pay pot increase that left those eligible at the mercy of line managers' discretion.

It said there was 95% support in favour of industrial action among maintenance, parlours and security personnel and it would look to escalate the dispute to other departments unless the Bank resolved the issue.

Unite said the ballot showed staff were angered by a below inflation pay offer for the second year running, claiming up to a third would get no pay rise this year at all.

The union's regional officer Mercedes Sanchez said: "Staff at the Bank of England have made their anger clear by voting for strike action due to their employer's outright refusal to negotiate a fair pay deal for its workforce.

"The Bank of England now faces its first strike action in over 50 years when staff in vital services across the country will be taking action because of the Bank's total refusal to accept that their workforce are struggling to meet their costs of living.

"The result of the Bank's unwillingness to negotiate fair pay will be that the Bank's sites, including the iconic Threadneedle Street in the city of London, will effectively be inoperable without the maintenance, parlours and security staff."

A Bank of England spokesperson said: "The union balloted approximately 2% of the workforce.

"Should the strike go ahead, the Bank has plans in place so that all sites can continue to operate effectively.

"We will continue to have discussions with Unite and hope that there will be a positive outcome."

Italy swoops in to save another bank leaving taxpayers on the hook for over $25 billion

Italian state has now guaranteed taxpayer money for a third bank in just over a week

Struggling BMPS launched a fully-fledged restructuring plan Wednesday morning

Controversies continues over European Commission approving bailouts

Gemma Acton | @GemmaActon
5 Jul 2017

The Italian state has stepped in with funding to save yet another failing bank, meaning taxpayers now stand responsible for over 22 billion euros ($25.4 billion) of bailout money recently extended to the sector.

Finance Minister Pier Carlo Padoan announced late Tuesday that the government had received approval from the European Commission to pump 5.4 billion euros into Banca Monte dei Paschi di Siena (BMPS) in exchange for the lender undertaking a major restructuring overhaul.

BMPS revealed an outline of its new 2017 – 2021 plan on Wednesday morning which it says will deliver a net profit of over 1.2 billion euros and a return-on-equity of over 10 percent by 2021. Management has committed to implementing a headcount reduction of around 5,500 and to close around 600 of the bank's existing 2,000 branches as well as a pay cap for senior management. BMPS also said that its CET1 ratio (its common equity tier 1 ratio which is a key standardized measure of a bank's financial strength) should reach 14.7 percent by 2021.

Toxic assets are at the heart of the bank's demise and its plan includes the intention to sell down 28.6 billion euros of gross non-performing loans (NPLs), of which 26.1 billion euros will be securitized (converted into marketable securities).

The move comes barely more than a week after Italy again received support from the European Commission for its pledge of a state guarantee of up to 17 billion euros as part of a plan to dismantle two troubled Venetian banks.

The use of taxpayer money to resolve problems within the banking system and therein protect retail bondholders in all three banks has been highly controversial given it flies in the face of the European Commission's commitment to avoid bailouts and all of the recent legislation that it has passed geared towards that purpose.

The banking sector has been struggling for years under the weight of a mountain of bad debt, and defenders of the state aid say the government's and the Commission's broader aim of lowering systemic risk validates the decision.

Additionally, the goal of shoring up the wider Italian financial system is now making progress, according to analysts at Citi.

"The stock of NPLs in Italian banks' balance sheets is significant but, given recent system developments, it is expected to show a large decrease before year-end," said Azzurra Guelfi, banking analyst at Citi in a note on Wednesday morning.

Furthermore, having bought into the new equity at a discount, the state could even stand to benefit from the BMPS transaction, says Gildas Surry, senior analyst at Axiom Alternative Investments.

"Over the next five years, definitely the state has a case where potentially it could get a good return on its investment," Surry told CNBC on Wednesday.

Indeed, there could also be an opportunity for brave investors, suggests Surry, if Italy follows the path trodden by Spain which has seen its banking sector shrink from around 70 lenders to closer to a dozen since the financial crisis.

"Potentially BMPS is a consolidation play because ultimately the bank will be clean and definitely there is consolidation to take place in Italy from the 400-plus institutions down to probably 150," he offered.

Defaulters may follow Essar route to block bankruptcy

BY SALONI SHUKLA & SANGITA MEHTA, ET BUREAU | JUL 06, 2017

THE ECONOMIC TIMES

MUMBAI: A number of large loan defaulters may follow the footsteps of Essar Steel by approaching courts to block bankruptcy proceedings against them, after the steelmaker got a stay on hearings on an insolvency petition moved by a bank.

Essar Steel is among a dozen defaulting companies identified by the Reserve Bank of Indiafor speedy recovery under the Insolvency and Bankruptcy Code, after the regulator was empowered by the government to direct lenders to take action against defaulters. Hearings in the RBI-identified cases started at the National Company Law Tribunal (NCLT) last week.

On Tuesday, Essar Steel filed a 'special civil application' in the Gujarat High Court challenging the proceedings initiated by Standard Chartered, seeking its intervention on grounds that the company was discriminated against by the RBI and lenders since they have given other defaulters six months to come up with a restructuring plan. On the plea, the high court stayed further hearings in the Essar Steel case before NCLT's Ahmedabad bench.

Lawyers said while the new recovery law does not give powers to civil courts to stall bankruptcy proceedings, the companies may approach courts alleging discrimination, as Essar has done.

"I think each company has different circumstances but these borrowers can challenge the RBI circular because the RBI has handpicked these 12 companies over other defaulters," said Nishit Dhruva, managing partner at law firm MDP & Partners.

In a communication on June 15, the RBI advised banks to initiate insolvency proceedings against Bhushan Steel (Rs 44,478 crore), Lanco Infra (Rs 44,365 crore), Essar Steel (Rs 37,284 crore), Bhushan Power (Rs 37,248 crore), Alok Industries (Rs 22,075 crore), Amtek Auto (Rs 14,075 crore), Monnet Ispat (Rs 12,115 crore), Electrosteel Steels (Rs 10,274 crore), Era Infra (Rs 10,065 crore), Jypaee Infratech (Rs 9,635 crore), ABG Shipyard (Rs 6,953 crore) and Jyoti Structures (Rs 5,165 crore). The NCLT has so far admitted Jyoti Structures' case for insolvency proceedings.

People dealing with some of the defaulters on the RBI list said they may also consider approaching courts. The companies themselves didn't make any comment.

All of Essar Steel's lenders have classifed their loans to the company as bad. State Bank of India, the lead bank, has received consent from 89% of the lenders to initiate insolvency resolution proceeding on Essar Steel. StanChart has opted to pursue its case separately.

In its petition, Essar Steel contended that it had cleared Rs 3,467 crore of dues and argued that an admission by the NCLT of the insolvency application would transfer the administration of an otherwise healing company into the hands of an interim resolution professional.

The steel company also challenged setting March 2016 as the cut-off date for defaults as it does not take into development thereafter. While bankers say that as long as the company is classified as in default they have the right to approach the NCLT for recovery of arrears, lawyers say that the resolution of these non-performing assets may happen only after a long protracted battle.

"Other borrowers short-listed by the RBI will also take this opportunity; why not? Soon we may start seeing others also challenging the RBI circular," said Meenakshi Iyer, partner at Advaya Legal. "This is a question of an entire company being wound up so these borrowers are likely to fight tooth and nail against it."

Canara Bank's exposure to 12 major defaulters is Rs.10,200 crore: Sharma

6th Jul 2017
BY REEMA TENDULKAR, SURABHI UPADHYAY, ANUJ SINGHAL

Rakesh Sharma, managing director and chief executive of Canara Bank, comments on the outlook for the lender, making additional provisions as directed by the Reserve Bank of India (RBI) and capital requirements for the additional provisions. Edited excerpts:

Lots of issues to discuss with you from the bank itself to overall debt resolution and recapitalisation requirements. So let me start off with a headline that we got last night with Essar Steel moving court against recapitalisation. Your thoughts on what this implies, whether it will have a ripple down effect and whether it is going to delay proceedings at the IBC?

I have also read the news. Basically now they have gone in their wisdom and filed petition. The matter is sub-judice so it will be not be proper for me to comment on this.

I am not asking about this specific case, I am asking a wider general question, do you see this impacting behaviour with respect to a lot of the other accounts as well and how legalities are then going to stack up if we see more challenges in the court?

I do not foresee any problem because IBC (insolvency and bankruptcy code) is there and as per that plan we have to file the cases with National Company Law Tribunal (NCLT) and there is a time-bound plan —180 days which can be extendable up to 270 days. I think the resolutions will come within 180 days. I do not foresee any delay in this, in fact the decision given by the Reserve Bank of India (RBI) is good, basically the timebound resolutions plan will happen and we will be able to provide the solutions.

As a result what will happen is the banks will be able to book interest income in this case. One thing we have to appreciate, all these are operating assets, not that the projects are stalled one. So operating assets are there, of course there have been some overleveraging, some cash flow problems have been there.

So once the solution is provided with the committee of creditors, I think this will be a positive thing to happen Since we are on the subject, could you tell us what the exposure of Canara Bank is to the 12 stressed accounts as identified by the RBI and what the provisions are that you have already made and what the incremental provisions then which would be required?

Our NPAS (non-performing assets) are Rs.34,000 crore as on 31 March 2017 and these 12 accounts which have been identified, we have exposure of Rs.10,200 crore which constitutes roughly 30% of our gross NPAS.

So in one way I see it as a positive as I said earlier and the resolutions will happen in my 30% of NPAS.

As far as provisions are there, we are already holding because all these assets are already NPA in various categories; some are in D1, D2 and we are holding, on an average, 35% of provisions in this. Of course our provision coverage ratio (PCR) was 55% as on 31 March but on specific accounts we are holding around 35-36% provisions.

So additional will be only 15-17% because these are all operating assets and the secured portion is 98.5%, so not that we will be required to make 100% provision on 50%.

This in normal case, I do not think any additional provision—because in normal cases when ageing process happens, we have been making the provisions like last year our PCR was 50% as on March '16, which increased to 55.62% as on March '17. So we had made additional provisions. So the bank has the capacity that we can absorb these provisions quite comfortably.

You are at 35% right now with respect to your exposure to these accounts, you need to bump that up by 15-17% as you said. Is that going to happen in Q1 itself?

RBI has given time up to March 2018. In fact, the instructions are that in next three quarters we can make. So depending on the profits rather instead of three, we have four quarters with us. So this will be like last year our operating profit was Rs.8,900 crore. We had made a provision of

Rs.7,500 crore. The slippages which had happened, we were required to make only Rs.1,700 crore provision. Remaining was to build up our PCR. So this addition of Rs.5,000 crore provision was there. So this year, around Rs.2,200 will not be a problem because it will be spread over the period of three-four quarters. So comfortably we will be in a position to absorb it. This incremental provisioning of 15-17% that you speak of, could you give us an absolute numbers roughly how much provisioning would that be? Roughly Rs.2,100 crore additional provision will be there.

Would you by anyway require capital to make these provisions from the banks, if you could walk us through what the capital situation of the bank is if the profits turn out to be inadequate?

I would like to mention two-three things. One is induction of raising capital, it can be in the form of equity tier-i and tier-ii and second is that capital conservation plan. During last two-three years we have adopted various measures as a result of which our risk weighted assets have come down. We have reframed our credit portfolio.

As on 31 March 2014 the risk weighted assets to total was 102%, which has come down to 95% as on 31 March 2017.

AIBEA THIS DAY – 9 JULY	
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