INSTITUTE OF BANKING STUDIES

IBS VIGYAN

VISIONING BANKERS

Evangelistically Speaking

Dear Stakeholders,

The New Year gave me some time to ruminate on the transformative advent of artificial intelligence (AI) in banking. By now, most users would have been familiar with the chatbot that pops up, offering assistance when you log in to an online marketplace. This is one fallout of the use of AI in enhancing customer experience. Chatbots have graduated to don the role of conversational assistants.

AI is not just about enhancing customer experience. As it can draw patterns from existing data and predict certain behavioural responses, it can find applications in wealth management and investment advisory services. Similarly, it is capable of automating processes that turn banks to be capable of handling larger volumes at lesser cost and higher efficiency.

Application of AI comes with a package of machine learning, natural language processing and computer vision. As it strives to read patterns for predictive analytics, people conveniently adduce the term "Intelligence" to its output, which may be a misnomer. But this capability is better put to use in identifying frauds. Any unusual type of transaction or destination of funds is promptly put to higher scrutiny to prevent frauds.

AI has found application in credit processing and decision support tools. But the human intervention is best retained as a need-based option while developing such algorithmic applications so that model risk is minimised.

Some banks have put this to use in regulatory compliance areas also. The fintech industry is poised to be one significant adopter of AI in their products and services.

As the data base from which the machine draws its "intelligence" is man made, the human bias in AI is unavoidable. All industries that put to use AI must be conscious of this inbuilt bias that creeps in unobtrusively.

A McKinsey report estimates the value of AI based development to touch $ 1 trillion soon, something that our country aspires to reach sooner. So, the impact of AI is going to be humongous. Several universities have added AI based elective papers in their curriculum, which reflects the demand that is emerging from the industry.

As AI makes ineluctable inroads into banking, the day is not far away when the certificate examinations of IIBF also include these developments in their skill upgradation schemes. So, let us embrace it at the earliest than being forced to do so later.

Looking forward to a sustaining engagement with all.

Sincerly yours

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Curated Cube

Does dividend drive stock price? If you believe in this correlation, RBI has published draft guidelines on declaration of dividend by Banks and repatriation of profits by foreign Banks. The primary condition to be eligible to declare dividend is that the bank must have met minimum regulatory capital requirements. Secondly the Bank's Board must also recognise any qualifications of the Auditors as well as "Emphasis of Matter" in their reports that could impinge on profitability or highlight revenues of one-time nature during the year, that merits derecognition. The dividend payout is capped at a range between 50% to 15% of profits, depending on the level of Net NPAs, whether it is at zero or 6%. Banks with NNPA above 6% are expected to utilise the profits fully for shoring up their loan loss provisions.

In another development, RBI has permitted Infrastructure Investment Trusts (InvIT) and Real Estate Investment Trusts (REIT) to issue Commercial Paper. The issuer of CP is now permitted to buyback after seven days from issuance against thirty days as stipulated in the 2017 Master Direction. Buyback of NCDs with contracted maturity less than one year is permitted after ninety days of issuance.

The RBI Governor, in one of his keynote addresses recently, has acknowledged that the resolution under the Insolvency and Bankruptcy Code has met with 35% success, either through full resolution or through withdrawal of process emanating from recovery.

He has flagged "Group Insolvency" as one of the issues to be addressed going forward. While some jurisdictions have adopted substantive consolidation approach, others have gone by procedural coordination approach. Under the former, the assets and liabilities of all group entities are realised together, while under the latter, the individual entities are treated independently but only procedures relating to documentation like filing requirements, timelines and coordination are aligned across the group entities. Presently banks in India are moving as per court directions relating to group insolvency. RBI aspires to address definition of group entity, intermingling of assets and cross border aspects to enhance the effectiveness of IBC. Securitisation of stressed assets is also in their agenda that would pave way for a vibrant secondary market for stressed assets.

RBI's draft guidance note on recognising Self-Regulatory Organisations for Regulated Entities is a welcome initiative. Entities like FEDAI, FIMMDA, AMFI and PDAI have imprinted their mark as SROs. RBI desires the SROs to evolve on their own, gain credibility and acceptability and shoulder responsibilities like governance standards and enhanced conflict resolution mechanisms among member institutions.

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

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FOURTH PILLAR

CONNECTED LENDING: Connected lending means a process by a person or firm that can control or influence a lender to get loan for himself or his related parties and group companies at favourable terms and conditions. Such lending can involve moral hazard issues leading to compromise in pricing and credit management. These loans can subsequently become bad assets.

INSURANCE OMBUDSMAN LIMIT HIKE: Earlier the maximum compensation amount was capped at ₹30 lakh to policyholders, which has since been increased to ₹50 lakh.

DOMESTIC SYTEMICALLY IMPORTANT BANKS (D-SIB): The Reserve Bank of India issued its list of Domestic Systemically Important Banks (D-SIBs) on 27th Dec 2023, in which it moved State Bank of India (SBI) and HDFC Bank to higher buckets, while ICICI Bank continues to be in the same bucketing structure as last year. SBI shifts from bucket 3 to bucket 4 and HDFC Bank shifts from bucket 1 to bucket 2, while ICICI Bank stays in bucket 1.

RBI EXPANDS ISSUER ELIGIBILITY FOR COMMERCIAL PAPER: Currently, the CP market is dominated by big corporate issuers who are rated higher by CRAs. Corporates, NBFCs and brokerage firms account for close to over 80% of CP issuances. The RBI has recently allowed infrastructure investment trusts (InvITs), real estate investment trusts (REITs), cooperative societies and limited liability partnerships to raise funds via CPs. The new directives will take effect from April 2024.

PENNY DROP VERIFICATION: The Pension Fund Regulatory and Development Authority (PFRDA) has made “penny drop” verification mandatory for all NPS fund withdrawals. Penny drop is an account verification method that involves depositing a small amount in a subscriber’s bank account for authentication before crediting funds to the beneficiary. This verification process ensures the accurate and secure transfer of funds to subscribers’ bank accounts during withdrawals and scheme exits.

INCLUSION OF SOVEREIGN GREEN BONDS UNDER FULLY ACCESSIBLE ROUTE: The Reserve Bank of India has recently issued a circular expanding investment opportunity for non-residents in the Government Securities market in which Sovereign Green Bonds has been included in the ‘Fully Accessible Route’ (FAR), opening new avenues for investors.

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

INQUISITIVELY SPEAKING

1. What is the Real GDP growth projected for 2023-24 in the recently concluded MPC meeting in Dec 2023?
a) 6.69% b) 6.75%
c) 7% d) 7.10%

2. What is the CPI inflation rate projected for 2023-24 in the recently concluded MPC meeting in Dec 2023?
a) 5% b) 5.20%
c) 5.40% d) 5.80%

3. The transaction limit for UPI payments for Retail Direct Scheme and for IPO subscriptions is ₹..... lakh.
a) 4 b) 5
c) 6 d) 8

4. UPI transactions for medical and educational services is likely to be increased to ₹... lakh as proposed by RBI in Dec 2023.
a) 3 b) 5
c) 6 d) 7

5. As per extant instructions of RBI, credit card receivables of scheduled commercial banks (SCBs) attract a risk weight of 125% while that of NBFCs attract a risk weight of 100%. On a review, RBI has decided to increase the risk weights on such exposures to ___% and ___% for SCBs and NBFCs respectively.
a) 130, 110 b) 135,115
c) 140, 120 d) 150, 125

6. As per RBI Master Directions on KYC/AML, the reporting entities shall preserve the documents of the transactions undertaken by walk-in customers for a period of ... years from the date of transaction.
a) 2 b) 3
c) 4 d) 5

7. As per regulatory measures towards consumer credit and bank credit to NBFC, RBI has decided to increase the risk weights in respect of consumer credit exposure of commercial banks including personal loans, but excluding housing loans, education loans, vehicle loans and loans secured by gold and gold jewellery, by 25% points to_____%.
a) 110 b) 120
c) 125 d) 150

ANSWER KEY

1.c 2.c 3.b 4.b 5.d 6.d 7.c

Stretch n Speak

CIRP: Corporate Insolvency Resolution Process

IRRA: Investor Risk Reduction Access

NeSL: National e-Governance Services Ltd.

WOS: Wholly Owned Subsidiary