

## **Banking and Finance – Sector Note, April 2019**

### **Background:**

In very simple terms it can be said that, the financial system of a country catalyzes economic development by transforming savings into investments, which in turn facilitates wealth creation. The financial services industry, of which banking is a major component, is impacted by the interplay of a host of factors like Technology, Regulations, Fiscal and Monetary policies, Trade relations and Tax policies. The sector has witnessed disruptive growth in India in recent years, by virtue of enablers like Big Data, Startup movement, Outsourcing, Differentiated banking licenses to name a few. Increased digitization and Government supported financial inclusion initiatives have also spurred innovation in product designing and distribution models for banking and financial services delivery. However, India's unprecedented climb to historic high levels of investment and saving rates in the mid 2000s has been followed by a pronounced, albeit gradual, decline. If we need to contain the investment slowdown, the pertinent short term policy agenda has to be revival of private investment. On the brighter side, the share of financial savings in aggregate household savings has already risen post demonetization. The soft interventions for business, like Easing the Cost of doing business & streamlining Tax, Regulatory & Environmental compliance and handholding the medium and small scale enterprises would go a long way in boosting the capex cycle in India.

The Department is headed by **Mr. Rajarshi Ghosh.**

### **Current Scenario:**

The banking and financial services sector in India primarily comprises commercial banks, payments banks, small finance banks, insurance companies, non-banking financial companies, co-operatives, pension funds and mutual funds. The Indian banking system

consists of 27 public sector banks, 21 private sector banks, 49 foreign banks, 56 regional rural banks, 1,562 urban cooperative banks and 94,384 rural cooperative banks and cooperative credit institutions. As of Q1 2018-19, total credit extended by commercial banks surged to INR 86,976.2 billion and deposits grew to INR 115,070.3 billion. India's retail credit market is the fourth largest in the emerging countries rising to INR 17941.8 billion on December 2017 from INR 11408.4 billion on December 2014. As per a Reserve Bank of India (RBI) report, the Indian banking system is on the cusp of a transformation, aided by recent policy measures to reduce vulnerabilities and improve its financial health.

The assets under management (AUM) of retail non-banking finance companies (NBFCs) in India witnessed a sharp slowdown in Q3 2018-19, as entities facing tightened liquidity moderated their incremental disbursements, according to credit rating agency ICRA. The agency said the AUM growth slowed to 3.3 per cent quarter-on-quarter (q-o-q) in Q3 2018-19, the slowest in the past 10 quarters.

According to a Crisil report, the total AUM of the Indian Mutual Fund industry rose 6 per cent to touch INR 24.51 lakh crore in the 2018-19. Mutual fund assets grew at the slowest pace in seven years, as debt funds, which constitute a major portion of the overall AUM of the mutual fund industry saw substantial outflows during the period. The industry continues to be highly concentrated, both geographically and in terms of fund houses, with the share of the top five and top ten fund houses being 58 per cent and 83 per cent, respectively, as of March 2019.

The latest IRDAI data shows that assets of non-life insurers grew by a healthy 21 per cent in 2017-18. Their AUM grew from INR 2.22 lakh in 2016-17 to INR 2.69 lakh crore in 2017-18. Private general insurers accounted for 36 per cent of the industry's assets in 2017-18. The total assets of the Indian life insurance industry reached INR 34 lakh crore while the AUM touched around INR 32 lakh crore in 2017-18. As on 31st March 2018, the total number of

branches of life insurers in India was 11,111; total direct employment in the industry was 2.65 lakh during 2017-18.

### **Future Outlook**

- Moody's Investors Services' outlook for Indian banks in 2019 is stable, as the pace of bad asset accumulation has slowed
- Funding and liquidity profiles of public sector banks will remain resilient
- AMFI sees mutual fund industry's AUMs growing to INR 94 trillion by 2025
- 2 per cent of the population in India is currently invested in mutual funds and ETF. This speaks for a huge growth potential in the segment
- Insurance Industry to play a pivotal role in India's growth story by offering innovative risk covers, policies and schemes
- Retail NBFCs likely to see improved liquidity in second half of FY 20

### **Policy level changes**

- The Reserve Bank of India (RBI) in April 2019 carried out a second successive interest rate cut in a span of two months while maintaining a neutral monetary policy stance. The central bank cut its benchmark repo rate by 25 basis points (bps) to 6 per cent.
- Insurance regulator IRDAI is planning to give policyholders an option to receive payment of claims in installments under certain specific policies like personal accident and benefit based health insurance.
- Association of Mutual Funds in India (AMFI) has modified certain provisions in its best practices circular on transfer of assets from one distributor to another
- SEBI has flagged 'outdated' recovery methods to sell attached assets