# Banks of future will be very different, says RBI governor

## Regulating the distinct segments of these banks would be a challenging task: Das

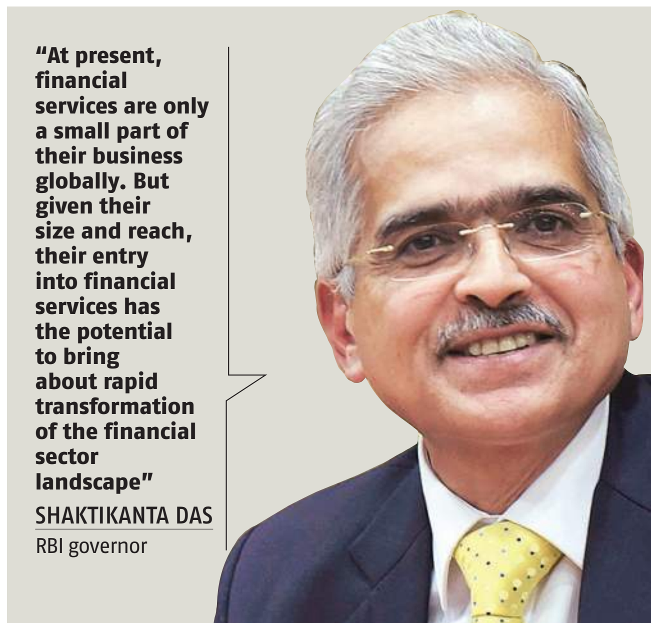
ANUP ROY
Mumbai, 24 February

Banks of the future would be extremely different from now, and regulating the distinct segments of these banks would be a challenging task, Reserve Bank of India (RBI) Governor Shaktikanta Das said on Monday.

Therefore, an integrated framework for resolution of financial firms operating in India could be expected in the near future as that would add to the resilience of the financial system, Das said at the annual banking event of *Mint*.

Financial technology companies (fintechs) are posing challenges to the existing banks, but big technology companies, or BigTechs, are also entering the financial services industry in a significant way. Some BigTechs are depending on their data-network activities, while venturing into payments, money management, insurance, and lending activities.

"At present, financial services are only a small part of their business globally. But given their size and reach, their entry into financial services has potential to bring about the rapid transformation of the financial sector landscape," Das said.




The entry of these firms have many potential benefits, and they can easily provide basic financial services to the masses at cheap cost, he said.

But the advent of fintechs and BigTechs are a challenge to banks, as well as banking regulators. While banks have to imbibe these new technology and business practices to remain competitive, banking regulators, on the other hand, Das said, "have to focus on achieving a balance between promoting innovation and applying a measured/proportional supervisory and regulatory framework."

"All these mean that the future of banking will not be a continuation of the past. We would see a very different banking sector, in terms of structure and business model, in the coming years," the RBI governor said.

There would be different categories of banks. The first segment could be large Indian banks with domestic and international presence, for which merger of public sector banks are already taking place. The second segment could be mid-sized niche banks, and the third segment could be smaller private sector banks, small finance banks, regional rural banks, and co-operative banks. The fourth could be of digital players, which may act as service providers directly to customers or through banks by acting as their agents or associates.

In any case, the conventional banking system would make way for next-generation banking, with a focus on digitisation and modernisation, where the need for brick-and-mortar branches would be reviewed continuously.

The decision by the National Payments Corporation of India (NPCI) to set up a subsidiary focusing on taking the Unified Payments Interface (UPI) model to other countries would help enhance global outreach of India's payment systems, the RBI governor said. A new umbrella entity for retail payments, for which draft guidelines have been released, would also intensify competition and further innovation in the retail payments space.

According to Das, despite the recent decline in impaired assets and a significant improvement in provisioning, "profitability of the banking sector remains fragile".

Even as capitalisation has improved, "the sector continues to encounter challenges from events like those around the telecom sector," he said. "Consequently, the overhang of non-performing assets (NPAs) remains relatively high, which is weighing on credit growth."

Banks now have shifted their focus away from large infrastructure and industrial loans towards retail loans, but this diversification strategy has its own limitations.

"Further, sector-specific pockets of stress need policy attention," the governor said, adding, proper due diligence and risk-pricing in lending are of prime importance so that health of the banking sector is not compromised while ensuring adequate flow of credit to productive sectors of the economy.

"As the Indian banking sector is propelled forward to a higher orbit, banks would have to strive hard to remain relevant in the changed economic environment by reworking their business strategies, designing products with the customer in mind and focusing on improving the efficiency of their services," Das said.

# Cash still rules but digital payments rising sharply

ANUP ROY
Mumbai, 24 February

**CURRRENCY IN CIRCULATION TO GDP %**

| Year | % |
|---|---|
| 2014–15 | 11.6 |
| 2015–16 | 12.1 |
| 2016–17 | 8.7 |
| 2017–18 | 10.7 |
| 2018–19 | 11.2 |

Source: RBI

Cash is still king in India, but there has been a perceptible shift in favour of digitisation in recent years, according to an internal study of the Reserve Bank of India (RBI).

Having a high currency in circulation (CIC) relative to gross domestic product (GDP) is a good indicator of cash being highly preferred for payments. Based on this assumption, "India continues to have a strong bias for cash payments," the study noted.

Demonetisation and an active growth in GDP brought down the cash in circulation as a percentage of GDP to 8.70 per cent in 2016-17. This increased to 10.70 per cent in 2017-18 and to 11.2 per cent in 2018-19 which, however, is less than the pre-demonetisation level of 12.1 per cent in 2015-16.

"The rate of increase is lower, indicating a perceptible shift away from cash," the report said.

The notes in circulation (CIC minus coins in circulation) increased at an average rate of 14 per cent between October 2014 and October 2016.

Assuming the same growth rate, notes in circulation (NIC) would have been ₹26 trillion in October 2019. NIC, however, was ₹22.3 trillion, indicating that digitaisation and reduction in cash usage helped reduce NIC by over ₹3.5 trillion, according to the report.

However, the cash withdrawals from ATMs increased over the past five years.

"India is next only to China in terms of the cash. However, the percentage of cash withdrawals to GDP has been constant in India at around 17 per cent," the report said, adding, with a compound annual growth rate (CAGR) of 9 per cent in terms of volume and 10 per cent in terms of value, the growth in cash withdrawals has been slow when compared to digital payment transactions, which grew at a CAGR of 61 per cent and 19 per cent in terms of volume and value, respectively. This indicated a shift towards digitisation.

Thus, "in India, like in many parts of the world, cash is the well-established and widely used payment instrument. It is, however, reassuring that non-cash payments, especially those using electronic or digital modes, are rapidly increasing."

# BofA expects RBI to build $550-bn forex reserves

ANUP ROY
Mumbai, 24 February

Bank of America (BofA) sees $550 billion as a comfortable foreign exchange (forex) reserve level for the Reserve Bank of India (RBI), and believes that the central bank will continue to accumulate dollars at every opportunity, even at the cost of a weaker rupee.

As of February 14, the RBI's forex reserves stood at $476 billion. The central bank has bought $49 billion in this fiscal year so far, more than offsetting the $15.4 billion sale in 2018-19.

According to BofA, the 'conservative' level of forex reserves for the RBI works out to be $550 billion.

According to BofA's economists Indranil Sen Gupta and Aastha Gudwani, there are three reasons why the RBI would want to accumulate more reserves — to maintain more import cover, fully covering foreign portfolio investors' investments, and to maintain a healthy cover on short-term external debt of India.

The one-year forward import cover has slipped to 11.1 months from 14.4.

"The reason it looks relatively high is that low growth has pulled imports to 16.4 per cent of gross domestic product (GDP) from the average 21.9 per cent since 2005-06."

To maintain import cover at 20 per cent of GDP, India would need at least $535 billion of forex reserves, the duo said.

Second, to maintain 100 per cent cover for FPI investments would require at least $520 billion. Finally, to take care of the short-term external debt and FPI's debt investments, India would need to maintain twice the exposure in foreign exchange. That works out to be $594 billion.

BofA sees rupee at 70.5 a dollar in March 2020.

# PayPal plans UPI-based e-payments

YUVRAJ MALIK
New Delhi, 24 February

On the heels of WhatsApp getting key approvals to launch digital payments in India, its US peer PayPal is also set to jump on the bandwagon.

One of the biggest international remittance services in the world, PayPal Holdings, Inc. will launch a peer-to-peer (P2P) payments feature in India, sources in the know of the company's plans said. The service is based on Unified Payments Interface (UPI) — India's indigenous digital payments network — and will roll out in the 'coming months'. The move pits PayPal right up against Paytm, Google Pay, PhonePe, and a few others, and comes at a time when digital payments adoption is on the rise. Transactions via UPI doubled in 2019; in 2018, it had grown five times.

This is the first time PayPal is experimenting with P2P. It has so far offered Indians the facility to transfer money to international bank accounts and pay at select merchant sites in India. A PayPal India spokesperson said: "As a policy, we do not comment on any market speculation."

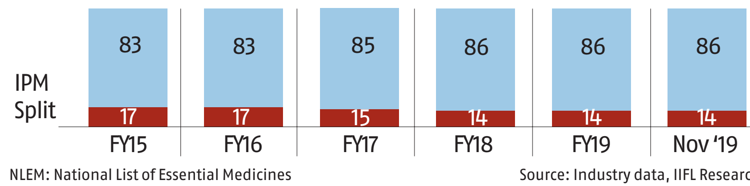
Experts said PayPal was perceived to be late in rolling out consumer payments. "India is going to be one of the biggest P2P payments markets in the world," said Mahesh Makhija, partner and leader-digital and emerging technology group, EY.

According to company figures, Paytm logs over 500 million monthly transactions, PhonePe 70 million, while Google Pay has amassed 67 million monthly active users. The competition will further increase when WhatsApp, which has 400 million users, will launch payments.

# Share of drugs under price control dips

SOHINI DAS
Mumbai, 24 February

**NLEM as a % of total domestic market has been coming down over the years**




NLEM: National List of Essential Medicines
Source: Industry data, IIFL Research

The share of drugs that are under price control in the overall domestic pharma market is showing a downward slide over the years. The data shows that from a 17 per cent share in 2014-15 (FY15), it as come down to 14 per cent in FY19. The trend remained the same during FY20.

During this period the Indian pharma market grew from ₹86,410 crore to ₹1.3 trillion, according to the data from market research firm AIOCD AWACS.

India follows a market-based mechanism for determining ceiling prices of medicines that are a part of the National List of Essential Medicines (NLEM). This list is updated from time to time by the National Pharmaceutical Pricing Authority (NPPA), the country's drug pricing regulator. The medicines that come under price control are known as scheduled drugs. For all other drugs, the firms are allowed to take an annual hike of not more than 10 per cent.

The data analysed by India Infoline (IIFL) shows that the share of drugs that fall under the NLEM as a percentage of the overall domestic pharma market is shrinking. "Only 14 per cent of the drug market by value is under price control at present," IIFL said.

The brokerage felt that multinational drug firms are at a disadvantage, compared with Indian peers when it comes to drug price control. This is because their products are priced at a premium to the market and in the event of any ceiling fixation, MNCs have to bring down their prices much more than the others, it said.

"Secondly, the rate of product launches in MNCs is significantly lower, compared with Indian companies. So, the effect of the price control risk is likely to linger for MNCs. While larger brands provide better profitability, a price control would naturally have a disproportionate impact on companies that own larger brands," it noted. Indian firms, on the other hand, have shown themselves to be more nimble in switching prescriptions to non-price controlled products after price controls were brought in. This is reflected in the number of brand launches slowing over the years, as firms chose to rationalise their portfolios. From 3,836 brands being launched in FY15, it slowed to 2,663 brands launched in FY19, the data from AIOCD AWACS showed.

Dermatology, vitamins-minerals-nutrients, and gastroenterology are the leading areas in brand launches.

Leading pharma firm Cadila Healthcare had pulled out 100 tail-end brands from the market in 2018-19, even as it launched 50 new brands.

"One cannot stop production of brands that feature in the NLEM, but they can always reduce the volumes of these products by a certain amount every year. Thus, the volumes are reduced and eventually in a strategic move the companies weed out the brands that are low volume and low margin," said a senior official of an Ahmedabad-based drugmaker.

Recently, the Economic Survey of 2019-20 brought out an anomaly in India's price control mechanism. It said, "The regulation of prices of drugs through the Drug Price Control Order (DPCO) 2013, had led to increase in the price of a regulated pharmaceutical drug vis-à-vis that of a similar drug whose price is not regulated."

While pharma lobby groups have challenged the methodology used by the Economic Survey to arrive at such a conclusion, the industry as such was of the opinion that market forces can keep drug prices under check.

The managing director of a multinational drug firm that sells novel products in India said that it was time that the NLEM and price control were de-linked. "NLEM should be about accessibility and affordability of medicines. Market forces can keep prices under check," he added.

# Need sugar-ethanol price parity to achieve 10% blending: Experts

SANJEEB MUKHERJEE & AGENCIES
New Delhi, 24 February

India can achieve its 10 per cent ethanol blending target with petrol if there is price parity between sugar and ethanol, industry experts said on Monday.

In 2019-20 sugar season, ethanol blend with petrol is expected to be around 5 per cent, much less than the targeted 10 per cent by 2022, largely due to falling sugarcane production and improvement in price realisation.

Speaking at a two-day seminar on Sustainability Mobility-Ethanol Talks, organised by the Indian Sugar Mills Association (ISMA) and its Brazilian counterpart UNICA, global ethanol expert Plinio Nastari said a long-term price policy was required to define the ethanol-versus-sugar parity, which would give visibility to the investors for making investment to boost production capacity.

Lack of ethanol production capacity is the main hurdle in achieving the target. Brazil, the world's leading sugar producer, is a pioneer in ethanol blending with petrol and achieved more than 25 per cent.

Luis Henrique Guimaraes, president and chief executive officer of Raizen, one of the world's biggest ethanol producers, said global market for ethanol needed to be created.

Vivek M Pittie, president of ISMA, said India would find it difficult to meet its target of 10 per cent ethanol-blending with petrol just on the back of B- and C-heavy molasses. "It can only be achieved from direct ethanol production from sugarcane juice," said Pittie.

# 'No plans for listing as we do adequate disclosures'

The life insurance sector has grown at a healthy pace this year, but there is uncertainty over growth if slowdown in the economy persists. **TARUN CHUGH**, managing director and chief executive officer of Bajaj Allianz Life Insurance, spoke to **Subrata Panda** on the company's plans. Edited excerpts:

Q&A

**Has the insurance sector faced any headwinds because of economic slowdown?**

Not yet. Whatever has been happening this year has been good and consumers have been saving for life insurance. It grew at around 17 per cent and persistency for the sector has been strong. We have grown well above the industry average. But I don't know how long this will continue, given the fact that the economy is not doing that well.

**The company's focus has been life goals. How has that panned out so far?**

It's doing brilliantly, but I have a feeling that it will be a hedge against Section 80C. The insurance regulator, from February 1, has insisted on need analysis. For us, we already had the template. The thinking and orientation of the company itself was focusing on life goals of customers. With Irdai (Insurance Regulatory and Development Authority) insisting that every product sale has to be backed by need analysis, this has only helped us in bridging our gaps. We were earlier looking at savings as a life goal and wealth creation around that but now we are also pitching for clear life goal around term insurance.

**What is your plan to improve the persistency levels?**

There are some practical difficulties that are there. There is 100 per cent surrender value and no surrender charge. So, a long-term product can be played as a short-term one. And when we have products like ULIPs in the markets today, it is going to be tough to attain the 90 per cent persistency level. Also, not everywhere do we have clear information on customer details. Moreover, it also depends on the segments you are playing in. In the big cities, if you are playing in the affluent segment, then usually the persistency is very good. And products sold through bancassurance partnerships usually have a better persistency. We were largely an agency-driven distribution network. Now, the bancassurance part is going. We have tie-ups with Axis Bank, RBL Bank, and two NRI-based banks.

**The regulator had said insurers who have attained a certain size should ideally go for listing. Is your company planning an IPO?**

Not really. What we are doing instead is that in terms of our balance sheet, we are disclosing as much and sometimes more than what the listed companies are disclosing. The whole benefit of listing is when you require money or any larger interest from the shareholders on the governance issue. And, we are anyway disclosing everything and more because we are held by a listed company.

**Do you do yearly product reviews wherein the products that are not doing well are weeded out?**

Yes, we do. In fact, last week the review was highlighted to our shareholders and 60 per cent of our sales are happening through products that were introduced in the last two years. These are our goal-based products. And, the ones that are not doing well get discontinued. Irdai usually wants us to have lesser number of products. But invariably, all the companies have more than 30 products. The feeling is that we end up confusing the customers, but that's not usually the case. The world is at such a level that you need to keep trying new things. Child products is just 2-4 per cent of our entire sale. The sale of pension products is usually under 10 per cent of our entire sale.

**How is the online channel doing in terms of distribution?**

Online for us is over 10 per cent. And, the customer base is largely graduates, millennials and beyond. It is quite aligned to the life goal pitch and fairly concentrated in the larger cities. And a lot of traffic is coming from mobile.

# ExxonMobil, IOC and Chart join hands for virtual pipelines

ExxonMobil India LNG has signed a letter of cooperation with Indian Oil Corporation (IOC) and Chart Energy & Chemicals to establish a system of transportation infrastructure to expand gas access in India. Virtual pipeline systems deliver liquefied natural gas (LNG) by road, rail, and waterways to areas not connected by physical pipelines.

These firms will implement a gas infrastructure initiative that leverages LNG ISO intermodal containers to move gas as a reliable, cleaner, and cost-effective fuel.

A pilot project would be developed and a road map for mobile gas infrastructure expansion at scale will be created to improve access to an abundant and cleaner fuel source.

JYOTI MUKUL