FICCI-IBA Survey of Bankers

Issue 4

July – December 2016

Survey Findings – Summary

FICCI-IBA conducted the fourth round of Bankers survey for the period July to December 2016, which saw participation by 17 banks representing 52% of the total banking industry (by asset size) and includes public, private as well as foreign banks.

The survey was conducted in the backdrop of the demonetisation move with respect to specified bank notes (SBN), which has been unprecedented and expected to have short-term as well as long term implications for the economy, including the banking sector. All the participating banks in the current round of survey have welcomed the demonetisation move in light of its long-term benefits for the economy.

There has been a significant surge in CASA deposits of most banks post demonetisation, which has given a strong boost to liquidity and lowered their cost of funds. It has also encouraged banks to lower their MCLR across all tenures. In-fact, many banks have lowered the MCLR in the month of December 2016, despite no change in the repo rate by the RBI in its last monetary policy review. During the six month period July to December 2016, a majority (75%) of participating banks have reduced their MCLR by upto 30 bps, while almost 19% have reduced it by more than 40 bps. Most of the participating banks also expect their operating margins to improve.

The survey reveals that there has been a slowdown in credit demand as consumption has been affected in the short-term owing to cash shortage post demonetisation. However, many respondents expect credit demand to improve after 3-6 months, as economic activities are expected to pick up by that time.

Banks have also welcomed the increased emphasis on the digitalization of the banking services after the demonetisation drive and indicated that this will aid reduction in cost of transactions for banks over the long term. To further promote transition to a digitized and less-cash society, survey respondents have emphasized on the need for incentivizing the adoption of digital modes of payment. They also expect the government to take steps to strengthen the digital infrastructure and connectivity across the country. Suggestion has also been made to leverage post offices, public transportation, panchayats and district offices in furthering the implementation of digital drive for transactions.

From the banking sector's perspective, the respondents have identified specific measures to promote digital transactions. These include – enhancing penetration of banking facilities in unbanked areas and simultaneously creating awareness on various modes of digital transactions including their safety and security features; introducing innovative and convenient modes of digital payments, and building up capabilities to accommodate wide range of requirements for growing cohort of customers, in terms of products, higher skilled staff, interactive online channels, etc.

Survey Findings – Summary

Banks were also asked their views on regulating the fintech industry, that has seen rapid growth in recent times. Participating banks agreed that there is a need for monitoring and regulation of fintech industry to ensure customer protection. They believe that an appropriate body needs to be appointed as the regulator for fintech industry. Additionally, there need to be guidelines and regulations set for due diligence, data protection, cyber security and client protection. Other suggestions include mandatory Information Systems Audit for fintech companies, and a statutory requirement to keep a certain amount of cash with the regulator for resolving claims, if any.

For the upcoming Union Budget, banks expect the government to boost consumption demand and investment, by way of reduction in corporate as well as personal income tax, and by providing additional deductions under sec 80C and interest on home loans. Banks have also urged for enhancing the capital expenditure, especially for infrastructure. For the banking sector, the biggest demand is for additional capital infusion by the government in public sector banks, to provide a boost to credit growth. Other key suggestions include measures to fast track NPA resolution; creation of a Central Corporate Repository; and interest payment on CRR balance.

Amongst the industries and sectors that continue to see rise in credit demand, 53% of the respondent banks reported high demand from infrastructure sector, which is same as that in the previous round of the survey. The other key sectors which saw a rise in long term credit during July-December 2016 period included Real estate, Textiles, Auto components and Metals, Iron & Steel.

The survey also reveals that iron & steel, infrastructure and textiles continue to account for a large concentration of NPAs. For Infrastructure sector, while a majority of respondents (50%) have reported a rise in NPA levels during the period July-December 2016, 29% of respondents have in-fact reported a decline in NPA levels during this period.

On the whole, the number of banks reporting a rise in the level of NPAs is lower in the current round of the survey as against the preceding round. While 76% of participating banks reported a rise in the level of NPAs during the period July-December 2016, 85% had reported so for the preceding six month period. A large proportion of participating banks (44%) have also reported a reduction in requests for restructuring of advances during the period July-December 2016.

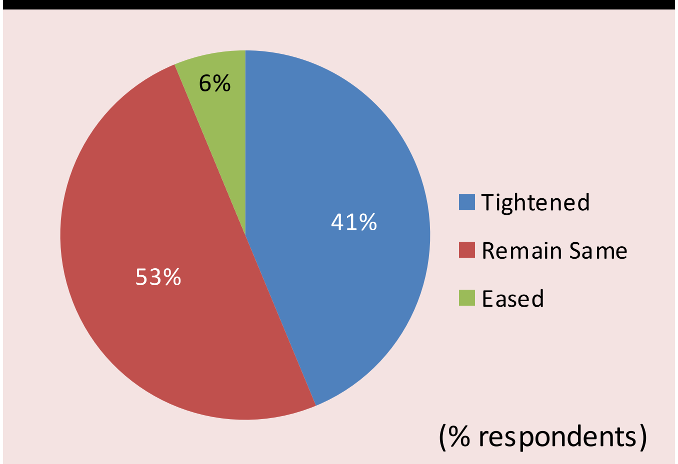
Going forward, the key sectors identified by the participating banks which could see a greater demand for long term credit include infrastructure (cited by 76% respondents), Automobiles (cited by 29% respondents) and Food Processing (cited by 29% respondents). Other sectors expected to see higher demand for long term credit include real estate, pharmaceuticals and textiles.

Change in Credit Standards

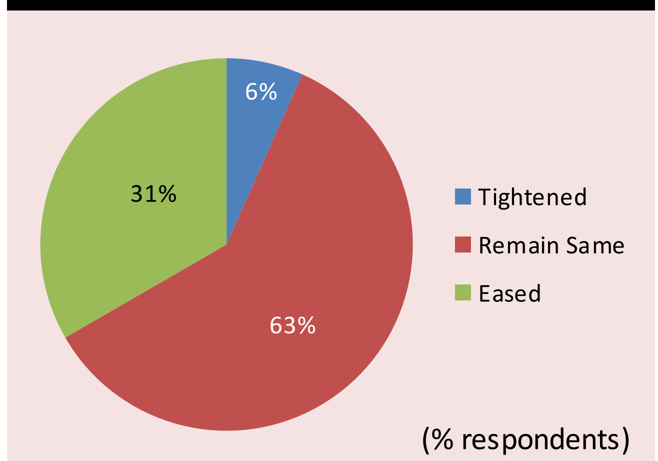
About 41% of the respondents have reported tightening of credit standards while lending to large enterprises during July-December 2016 period. This is the same as that reported in the previous round of the survey. 53% of the respondents, however, have reported no change in the credit standards.

For SMEs , a majority 63% respondents continue to follow the same credit standards as compared to the first half of 2016. However, 31% of respondents reported easing of credit standards. In the previous round of survey (January–June 2016), 16% of the respondent banks had eased their credit standards for SMEs.

Credit standards for large enterprises

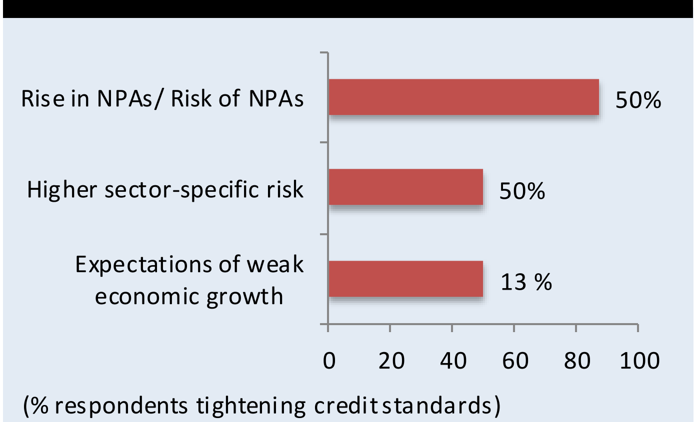


Credit standards for SMEs

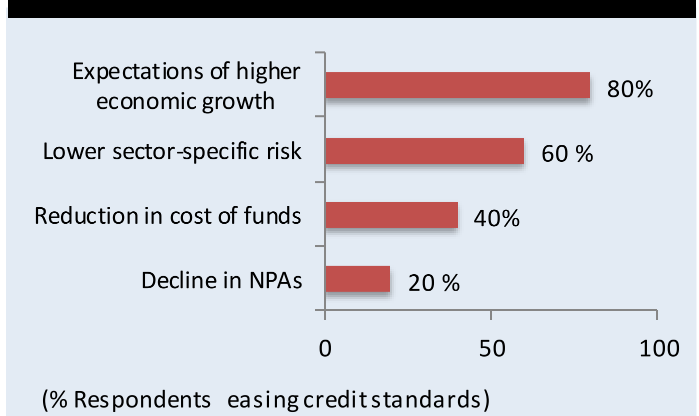


The respondents reporting tightening of credit standards for large enterprises have cited the key reason for same as the rise in the level of NPAs (reported by 88% of such respondent banks) along with higher sector specific risk and lower than expected economic growth (reported by 50% of such respondents). On the other hand, 80% of the respondent banks who have eased their credit standards believe that the economic growth will be high and 60% of such respondents attribute the change in risk perception to lowering of sector specific risk (mainly for SMEs).

Factors behind tightening of credit standards

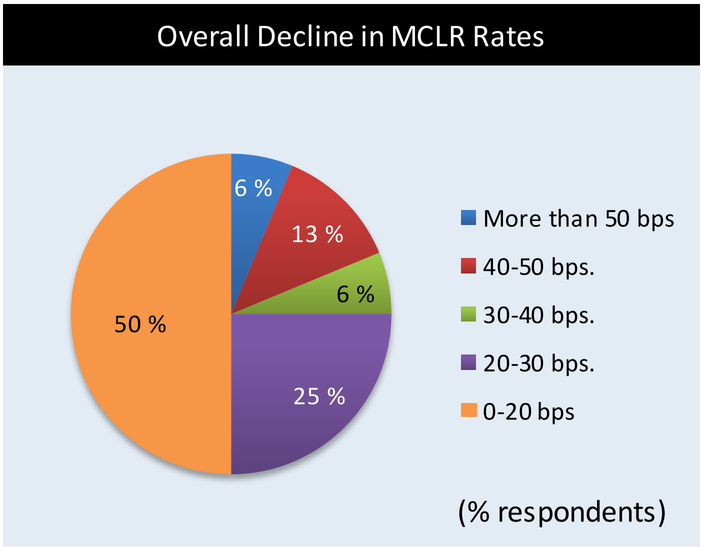


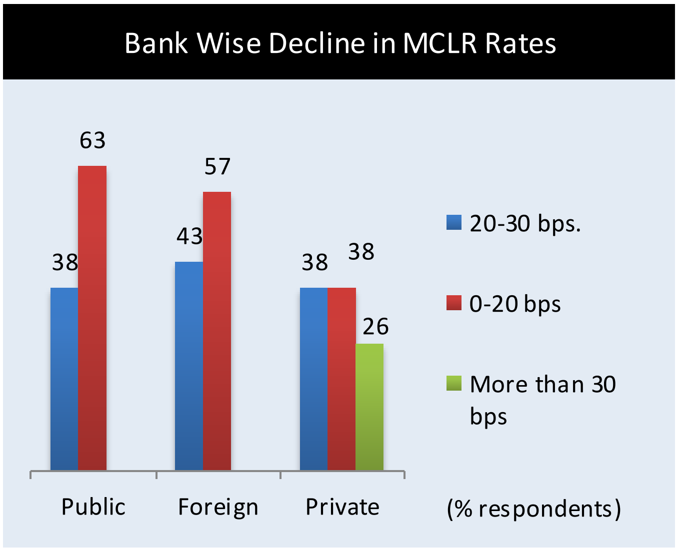
Factors behind easing of credit standards



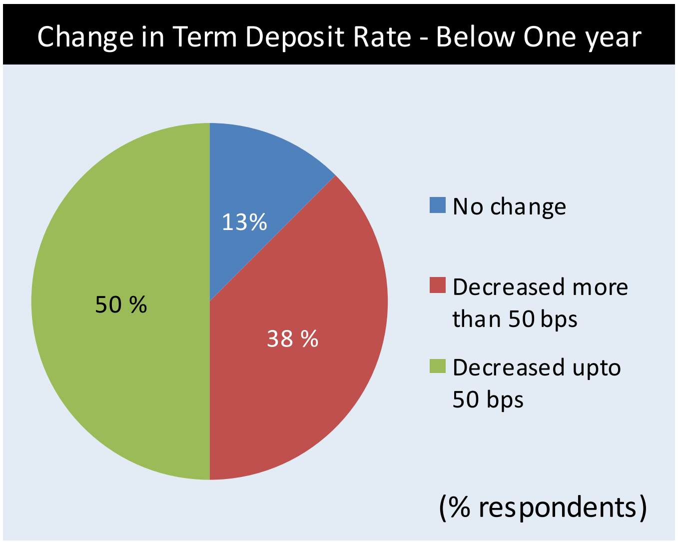
Movement in Marginal Cost of Lending Rates (MCLR)

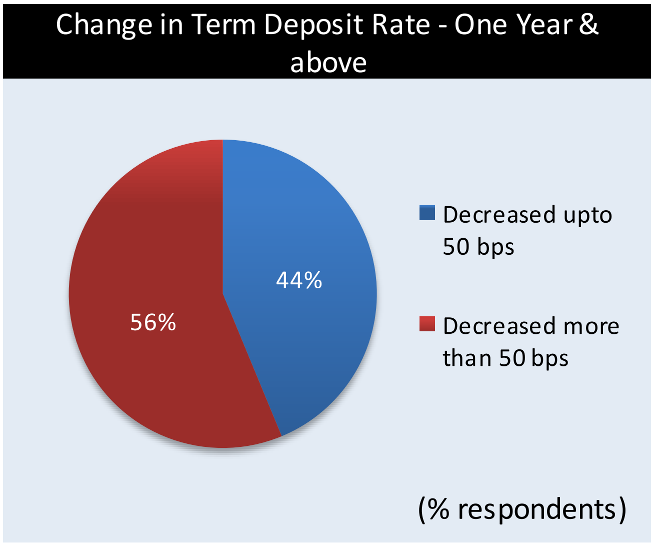
The Reserve Bank of India introduced Marginal Cost of Funds based Lending Rate (MCLR) with effect from 1st April, 2016. The new methodology uses the marginal cost or latest cost conditions reflected in the interest rate given by the banks for obtaining funds in the market. All the participating banks reported a decline in their MCLR rates in the current round. Amongst the banks that have reduced their MCLR in the July-December 2016 time period, 50% had reduced by 0-20 bps, 25% by 20-30 bps and 6% by 30-40 bps.





A majority of the respondent banks have reduced interest rates on term deposits. In case of short duration term deposits of less than one year, 88% of respondent banks had reduced rates. In case of long duration term deposits of one year and above, all the respondent banks have reported reduction in their term deposit rates. In the last round, 75% of the respondents had reported reduction in short duration term deposits and 90% of the respondents had reported reduction in long duration term deposits.



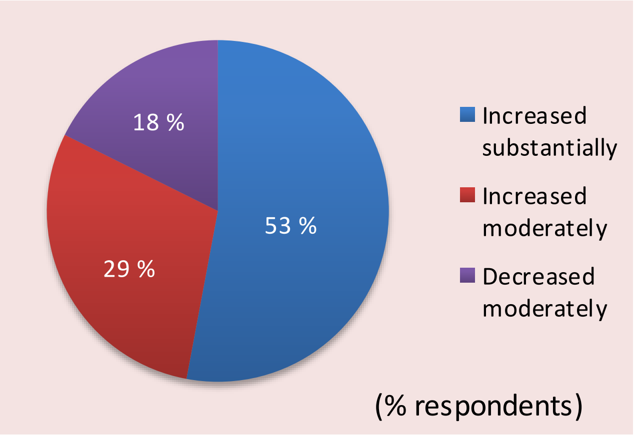


Changes in Current Account and Savings Account Deposits

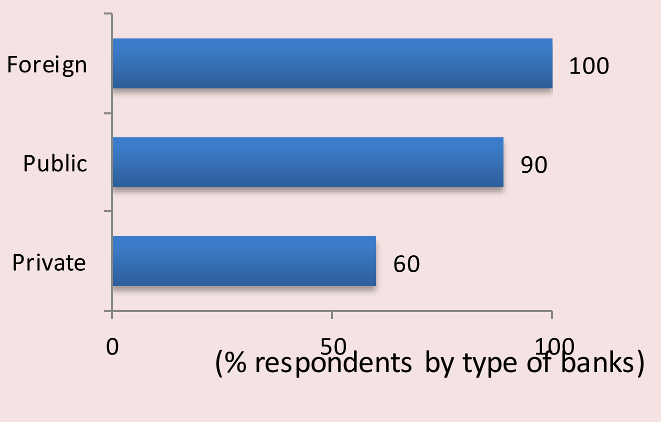
A majority of the banks (82%) reported a rise in their CASA deposits during the period July-December 2016. In fact, 53% of the respondent banks have reported substantial increase in CASA deposits and attributed the same to demonetisation move of the government, besides continuous efforts of banks to mobilize opening of savings account. In the previous round, only 25% of respondents had reported substantial increase, while 50% had reported a moderated increase in such deposits. It is pertinent to note that CASA increased substantially after demonetization.

A comparison across type of banks for this round of survey shows that all the reporting Foreign Banks witnessed a rise in their CASA deposits, followed by 90% of Public Sector Banks and 60% of Private Banks responding to the survey.

Change in share of CASA Deposits to total deposits



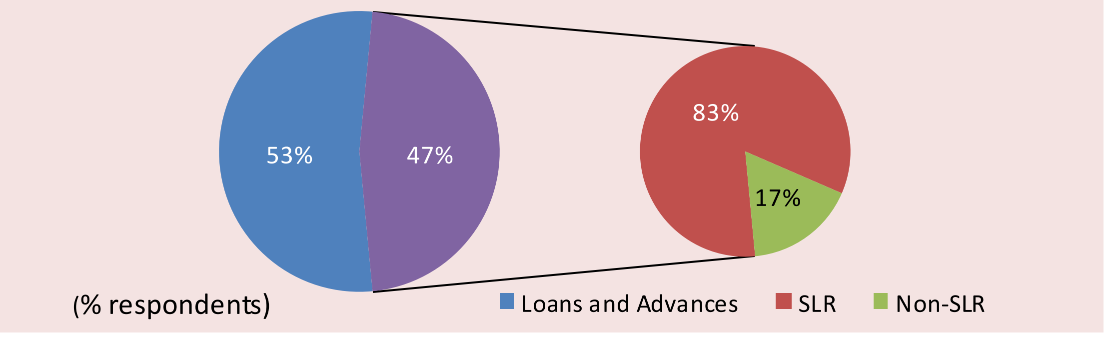
Bank-wise respondents reporting rise in share of CASA Deposits (%)



Composition of Funds Portfolio

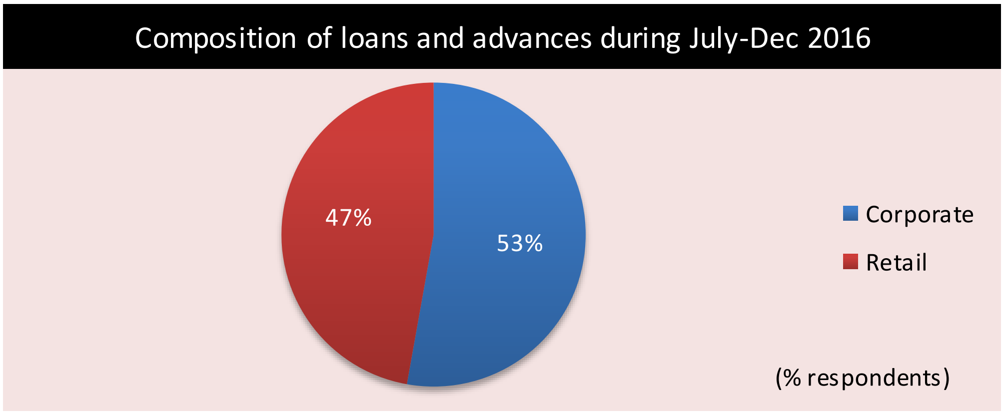
During the period July-December 2016, the participating banks had utilized on an average 53% of their funds towards loans and advances, and about 47% towards investments. Of the funds used for investments, the reporting banks hold a significant portion (about 83%) of their investments in SLR investments and 17% in non-SLR investments. This could be due to subdued demand for credit.

Banks Portfolio : Loans and Investments

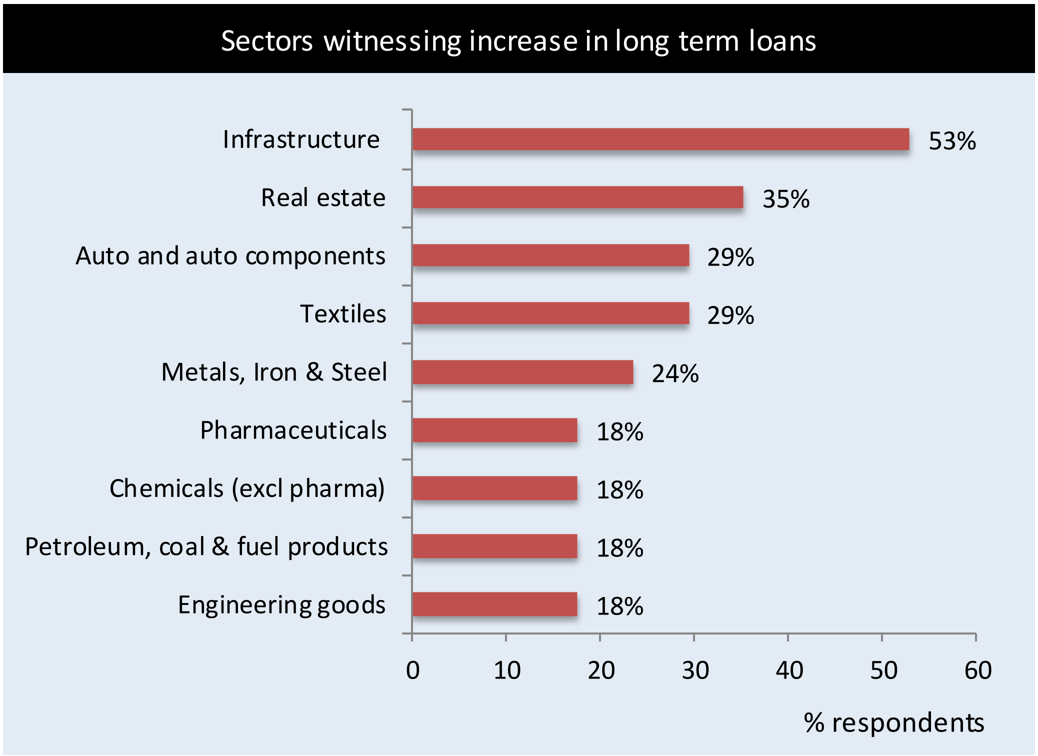


Composition of loans and advances

During the period July-December 2016, the corporate loans comprised 53% of total loans and advances of the participating banks as compared to 47% for retail loans. In the preceding round, the share of corporate loans and retail loans were 62% and 38% respectively. The increase in relative share of retail loans does indicates an increased focus from banks towards increasing their retail portfolio.



With respect to the growth in long term credit for specific sectors, there hasn't been much change from the previous round. In the current round, 53% of the respondent banks reported high demand from infrastructure sector, similar to the earlier round. The other key sectors which saw a rise in long term credit during July-December 2016 period included Real estate, Textiles, Auto components and Metals, Iron & Steel.

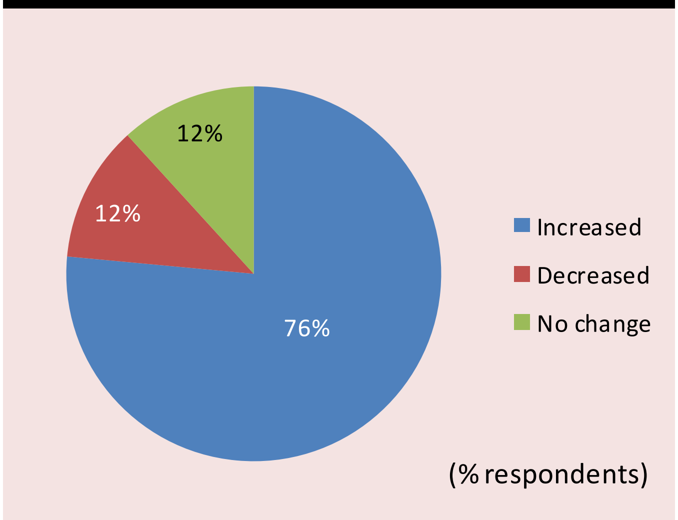


State of NPAs and Stressed Assets

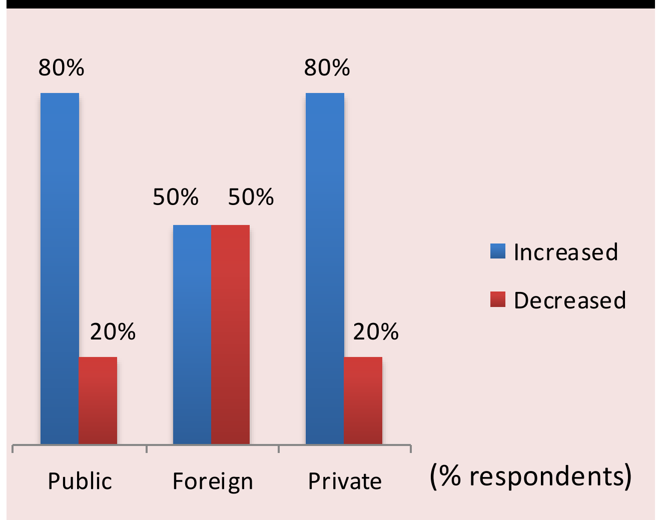
The number of banks reporting a rise in the level of NPAs is lower in the current round of the survey as against the preceding round. While 76% of participating banks reported a rise in the level of NPAs during the period July-December 2016, 85% had reported so for the preceding six month period.

In terms of Bank wise level of NPAs, 80% of the participating Private Sector Banks as well as Public Sector Banks reported a rise in their NPAs. This ratio for Foreign Banks stood at 50%.

Change in the level of NPAs



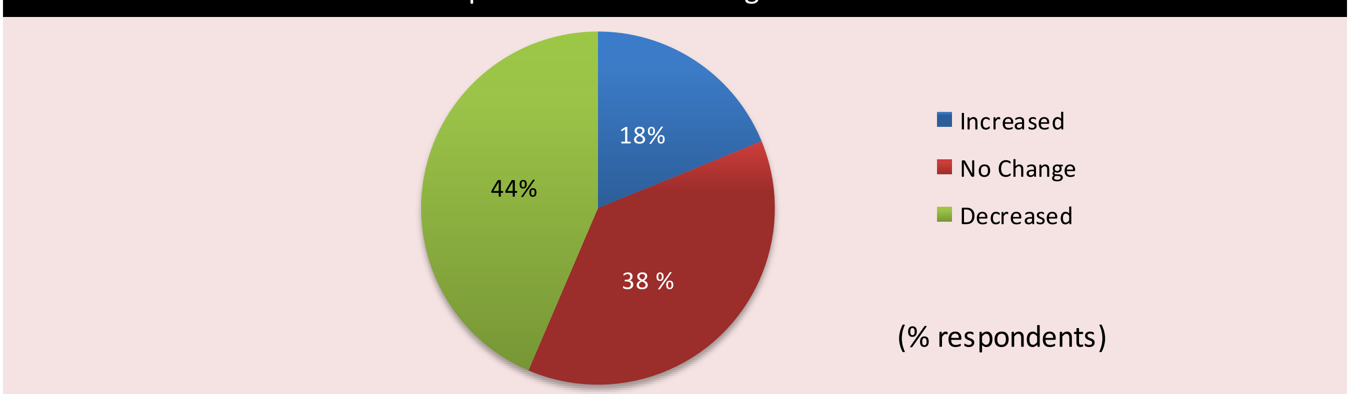
Bank Wise Increase/Decrease in NPAs



A large proportion of participating banks (44%) have reported a reduction in requests for restructuring of advances during the period July-December 2016. In fact, 60% of the participating Public Sector Banks have reported a reduction in such requests. In the preceding round, 47% of respondents had seen a decline in requests for restructuring, with 70% of participating PSBs indicating such decline.

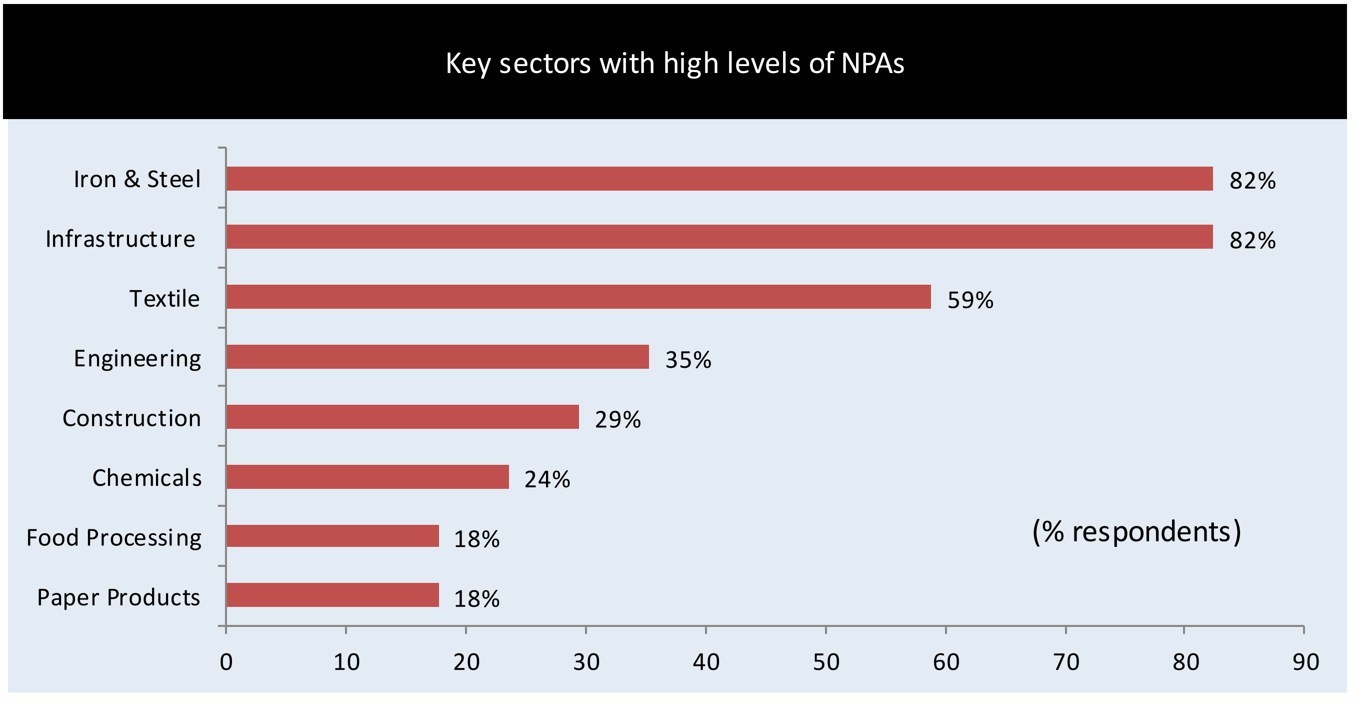
On the other hand, 18% of the respondent banks indicated a rise in the number of cases requesting for restructuring of advances as compared to 21% in the previous round.

Requests for restructuring of Advances



Key Sectors with High Level of NPAs

Similar to the previous round of survey, the latest survey also shows that the major sectors that account for largest NPAs amongst the participating banks include Iron & Steel, infrastructure & textiles. A large majority of respondents (82%) indicated Iron & Steel, Infrastructure (including power, telecom, road) as sectors with largest concentration of NPAs in their banks, followed by Textile (reported by 59% respondents), and engineering goods (reported by 35 % respondents).



<u>Trend in NPAs in key sectors</u>

- For Infrastructure sector, while a majority of respondents (50%) have reported a rise in NPA levels during the period July-December 2016, 29% of respondents have in-fact reported a decline in NPA levels during this period.

- For the iron & steel sector, 64% of the respondents have reported a rise in NPA levels in the second half of 2016, and about 29% have reported no change.

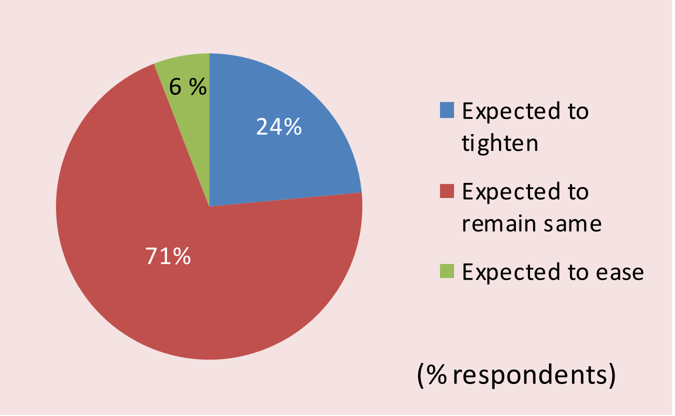
- Amongst the respondents highlighting textiles as one of the sectors with large concentration of NPAs, a significant 90% of the respondents reported a rise in NPA level and 10% have reported a decline.

- Likewise, in case of construction sector too, a high proportion of respondents (80%) have reported a rise in NPA levels.

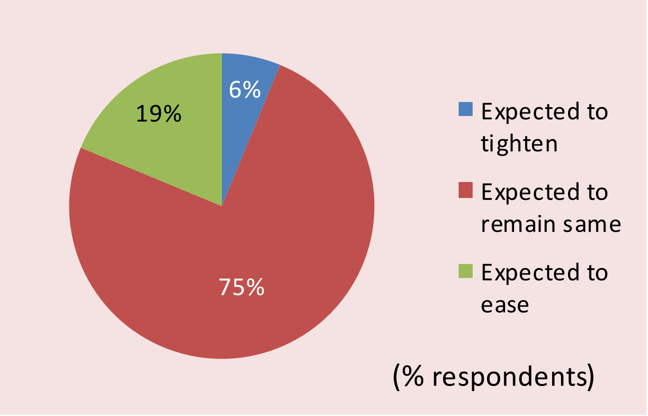
Expectations and Outlook on Credit

Majority of the respondent banks expect their credit standards to remain same for the period January – June 2017. However, 24% of the respondent banks have indicated tightening of credit standards for large enterprises going forward. With respect to the expected credit standards for SMEs, 19% of the respondent banks have indicated likelihood of easing of credit standards.

Credit standards for large enterprises

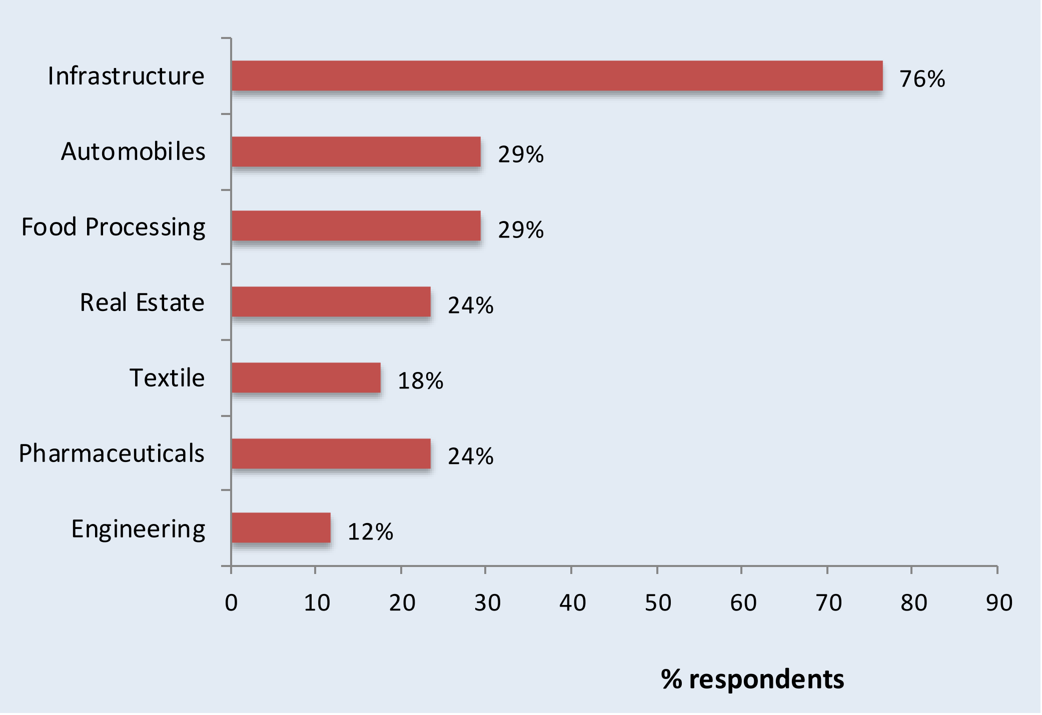


Credit standards for SMEs



The key sectors identified by the participating banks which could see a greater demand for long term credit in the first half of 2017 include infrastructure (cited by 76% respondents), Automobiles (cited by 29% respondents) and Food Processing (cited by 29% respondents). Other sectors expected to see higher demand for long term credit include real estate, pharmaceuticals and textiles.

Sectors expected to see rise in long term credit



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Indian Banks' Association

Expectations from forthcoming Union Budget 2017-18

General / Macro-economic Expectations of Participating Banks	***Reduction in corporate tax rates*** *and simultaneous phasing out of exemptions*
	Lowering of personal tax rates *as well as raise the tax exemption limit from current Rs 2.5 lakhs*
	Raise the ***deduction limit under 80C*** *of personal income tax to enhance domestic savings; deduction limit on interest on home loans should be raised*
	Enhance capital expenditure*, especially in infrastructure to create growth momentum*
	Additional ***incentives for digital transactions****, including tax benefits for customers as well as merchants*
	Increased ***focus on agriculture****; sops could include hike in interest subvention for farmers*

Expectations for Banking Sector	*Additional* ***capital infusion*** *by the government in Public Sector Banks, to enhance credit creation capacities of Banks and boost credit growth*
	Hike in FDI limits *for banking from the present 20% to 49%, as it will help in raising further capital and thereby meeting capital requirements under Basel III norms*
	Measures to fast track ***NPA resolution****, such as setting up of special courts, speeding up the full roll out of Insolvency and Bankruptcy Code. Banks have also suggested that all SARFAESI cases be disposed off within two years*
	Creation of a ***Central Corporate Repository****/ Credit Information Bureau to act as a single source for corporate data, which will help banks in credit decision making*
	Interest subvention (for farm loans) should be parked with the banks in advance*, as it takes 7-8 months for settlement of claims, leading to interest loss to banks*
	Additional ***tax incentives for customers on term deposits****; such as reduction in lock-in period for tax saver fixed deposits, and increase in tax exemption limit for interest income from term deposits*
	Interest to be paid on the CRR balance *with the RBI; there is a suggestion of at least 2% interest on CRR balance*

Views on Demonetisation and its impact on Banking Sector

	Positive Impact	Negative Impact
Liquidity	+ Boost to liquidity with rise in CASA deposits	
Cost of Funds	+ Lower cost of funds	
Credit demand	+ Improved credit demand in long term	− Short term slowdown in credit
Margins	+ Improvement in operating margins	

- Majority respondent banks have supported the demonetization move undertaken by the Government and the RBI. They believe that this is good for the economy over the long term.

- Participating banks feel that the full impact of demonetisation cannot be predicted at this juncture, but as of now, Banks have seen a surge in low cost CASA deposits.

- A large majority of participating bankers expect the cost of funds to come down and liquidity to remain comfortable.

- A large majority of banks believe that strong liquidity position and low cost of funds, will help them improve their operating margins. Some respondents have cited that earnings of banks could take a hit in third and fourth quarter of 2016-17, as revenue yielding business activities such as vending loans and cross-selling of investment products have taken a back-seat.

- Banks have also cited that increased emphasis on the digitalization of the banking services after the demonetisation drive, will aid reduction in cost of transactions over the long term.

- The participating banks have also highlighted that demonetisation drive has impacted the consumption demand in the short-term, thereby leading to slow down in credit demand as well. However, many respondents expect credit demand to improve after 3-6 months, as economic activities are expected to pick up post normalisation.

Suggestions to facilitate transition towards a less-cash society

Suggestions for Bank led initiatives to promote digital economy	*Enhance penetration of banking facilities in unbanked areas, simultaneously creating awareness on various modes of digital transactions including their safety and security features.*
	Banks need to innovate on new convenient modes of digital payments and attractively price these products to encourage adoption
	Align bank's technology and systems with national digital infrastructure that is being built (example UPI, Aadhar)
	Build up capabilities to accommodate wide range of requirements for growing cohort of customers, in terms of products, higher skilled staff, interactive online channels, etc.
	Regularly upgrade security systems to check cyber crimes and frauds

Suggestions for Government led measures to encourage digital transactions	*Government departments should bear the MDR costs and not levy surcharge on customers*
	Make digital invoicing mandatory for retailers with turnover above Rs 50 lakh
	Consider GST/ VAT/ Service tax deduction on digital sales by small merchants/ assesses
	Reduce corporate tax for start-ups promoting digital payment eco-system
	Introduce scheme for small value credit cards (up to Rs 10,000) without the need for CIBIL score
	Link all Post Office accounts to UPI/ IMPS/ digital cash networks; public transport to be enabled for UPI/ IMPS/ digital wallets
	Organise digital booths in rural areas and small towns through Panchayats and District Officials, with a view to impart digital training

Views on regulating FINTECH industry

The participating banks in the survey were asked whether there is a need to regulate fintech industry in India and if yes, what is the desired regulatory environment.
The respondents largely agree that given the rapid growth in fintech industry in India, there is a need for monitoring and regulation to ensure customer protection.

	Indicative suggestions by respondents on regulatory environment for fintech industry
Regulator	*An appropriate body to be appointed as the regulator for fintech industry*
Due diligence	*A minimum KYC standard should be set for fintech companies*
Cyber security	*Data protection regulations are essential. Failure to comply with such regulations should be addressed with strict penalties*
Client protection	*Guidelines should be set for protection of clients against any unlawful transactions. Provisions should be made to compensate client for loss/ damage on account of system failures*
Statutory reserve	*There should be a statutory requirement to keep certain amount of cash as reserve with the regulator for resolving claims, if any*
Audit	*Information System (IS) Audit should be made mandatory for fintech companies, and they should be scrutinised on the lines of Risk Based Supervision of Banks by the RBI*
Innovation	*As innovation is the key to success of any fintech company, the regulation should ensure that innovation in these companies is not hindered*

Respondents Profile

Seventeen Banks responded to the survey, representing a mix of public sector, private sector and foreign banks. Various indicators in the survey reflect information for the period July to December 2016. Expectations are for the period January to June 2017.