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## Personal

- Tell us something about yourself
    - Did my graduation in Mechanical Engg from ABC college – got placed in XYZ bank
    - Worked in Anti-Money Laundering team of Bank for 2 years after graduating in 2014. Mainly worked as team lead in implementing AML solutions for the flagship project of the bank
    - Have been preparing for CSE of UPSC for the last couple of years
- Why banking after engineering?
    - Offered job during placement
    - Goal civil services, did not want to take a break to study full time, hence decided to sit for placements
- Why RBI?
    - Given my experience of having worked in AML dept of a bank and desire to work in the public sector, RBI was a natural choice to apply for when I began looking for alternatives
    - While preparing for civil services, used to enjoy studying economics the most. All the concepts seemed very logical and I was able to grasp them quickly
    - Besides, RBI is one of the most reputed orgs in India and one of the few public orgs which commands the respect of the people
- Why civil services?
    - A career in civil services offers a chance to implement solutions to problems plaguing our society
        - Inequality of opportunity stemming from poverty and discrimination – I was fortunate that my parents could afford a good education for me but there are many people are not so fortunate
        - IT industry created by govt in Hyderabad
        - E-governance
        - Rangachari opened up insurance
        - Plague in Surat in 1994, it was a bureaucrat S R Rao who made the city one of the cleanest
        - Dr I V Subbarao – reduced waiting time at Tirupati from 3-4 days to a couple of hours
    - Challenges mean lifelong learning. Excellent way to pick up managerial skills and learning a lot about the country
    - Opportunity to work in a multitude of organizations, Ministries and levels in later years of career
    - Inspired by friends preparing for it
    - Social work
        - As a student with good academic record, was a mentor to students from my department who were struggling with academics
        - As the head of my dept's annual festival, launched a couple of initiatives like printing and distributing notebooks in govt schools and conducting workshops for school children in robotics – sponsored by money received from sponsorships
- How many attempts and why did you fail at civil services?
    - This year was 3$^{rd}$ attempt
    - Had not prepared much before 1$^{st}$ attempt – couldn't clear prelims; gave it in 2015
    - In 2$^{nd}$ attempt couldn't score well in Mains because I had to devote much of my time to my optional
    - This year I made some avoidable mistakes
- Will you sit for civil services again? If yes, why should be select you?
    - Will give one more attempt in 2019
    - Assure you that work will not suffer due to preparation. Already done with bulk of preparation and currently only have to update notes on a daily basis based on current happenings

    - Looking at facts, probability of my getting selected and leaving RBI seems low because number of candidates rising, vacancies falling and I have failed to clear thrice now
- How can engineering be used in RBI? What will mechanical engineer do in RBI?
    - Although the principles of mech will not be directly used in working for RBI, my training as an engineer has helped me develop an analytical mindset. When presented with a problem I try to find out the root of the problem and think of solutions
    - Moreover, in college participated in various extra-curricular activities. Was head of dept festival and managed a team of 10 Managers and participated in inter-hostel competitions
- Strengths
    - Biggest strength is my ability and more importantly willingness to analyze facts in a rational manner. Experiences invoke positive or negative feelings; try and analyze why these feelings and if they are correct; stereotype embedded in people, may even be true but there has to be a logical explanation to it
    - Attention to detail
    - Scared of getting into a comfort zone – preparation, tend to focus on subjects I like, can lead to decrease in productivity, hence shift to other subjects asap
- Weaknesses
    - Got to know a lot of my weaknesses from previous job
    - Outspoken – not very tactful/diplomatic when conveying disappointment
    - Perceived networking with senior functionaries outside of team as something negative and to be done to grab their attention for career growth – failed to see that it is an excellent opportunity to learn from more experienced people and learn about the latest happenings in the industry. This is something I will rectify when I join a new org
    - Hesitant in delegating tasks to experienced people, heavy workload on self
    - Nervous about speaking in a big group – silent listener at parties – but civil services preparation has helped because I have content now
- Opportunities
    - Opportunity in working in the public sector is that I will be working for the welfare of fellow citizens in a more direct manner instead of contributing to profits of corporates
    - The opportunity for job hopping within the org and even going out on deputation to other orgs ensures that I will continuously face newer challenges and continue learning
    - Eligibility criteria as well as exams conducted by RBI are quite tough and it will ensure that I will be able to work with bright minds of the country
    - Support and scholarships offered by RBI for higher learning opportunities
- Threats
    - Due to age and seniority issues, I may not be able to get promoted to policy making levels
    - Preparation for civils will not hamper work but may create a negative relationship with manager
- Most important quality - commitment

## Hobbies

- Reading fiction – have read many classics. Before beginning prep, was reading Alistair Maclean, Agatha Christie and P G Wodehouse. Last read Clive Cussler's Raise the Titanic
- Listening to old Hindi songs –listen to only those songs which I have heard someone playing; parents' influence
    - Kishore Kumar
        - Pyaar deewana hota hai – R D Burman – Kati Patang

        - Ye sham mastani – R D Burman – Kati Patang
        - Saamne ye kaun aaya – R D Burman – jawani deewani
        - Tere jaisa yaar kahan – Rajesh Roshan - yaarana
        - Mere saamne wali khidki me - R D Burman - padosan
    - Mukesh
        - Mera joota hai japani – Shankar Jaikishan – shree420
        - Kisiki muskurahaton pe ho nisar – Shankar Jaikishan - anari
        - Awara hun - Shankar Jaikishan - awara
        - Ek pyaar ka nagma hai – Laxmikant Pyarelal
    - Manna Dey
        - Ae meri zohra jabeen - waqt
        - Pyar hua ikrar hua – Shankar Jaikishan – shree420
        - Dil ka haal sune dil wala – Shankar Jaikishan – shree420
        - Ye dosti hum nahi - R D Burman - sholay
    - Mohammed Rafi
        - O mere sona re - R D Burman – teesri manzil
        - Gulabi aankhein - R D Burman – the train
        - Kya hua tera wada - R D Burman – yaadon ki baaraat
    - Asha Bhosle
        - Jaan e jaan dhoondta fir raha
        - O mere sona re - R D Burman
        - O hasina zulfon wali - R D Burman
- Kho Kho
    - Arjuna Award, **Eklavya Award for men, Rani Laxmi Bai award for women**, Veer Abhimanyu award for boys under 18, and Janaki award for girls under 16
    - Each team consists of twelve players, but only nine players take the field for a contest
    - two innings. An innings consists of chasing and running (defenders) turns of 9 minutes each
    - Eight members of the chasing team sit in their eight squares on the central lane, alternately facing the opposite direction, while the ninth member is an active chaser, and stands at either of the posts, ready to begin the pursuit
    - Defenders enter the limit, in batches of three
    - 29m by 16m
    - Single action of touching will not deemed as Foul. However, only uttering 'KHO' and do not touching a Chaser by hand, will be considered as Foul.
    - Kho kho featured in Asian Games for the first time in 1982 at Delhi
    - It was during the South Asian Federation Games in 1987 in Calcutta that the Asian Kho-kho Federation was formed, which later helped popularize *kho-kho* in Pakistan, Bangladesh, Nepal, and Sri Lanka
    - $1^{st}$ International Kho Kho Championship in England in Sept this year
    - Olympic Council of Asia recently gave recognition to kho-kho and it may be added to next Asian Games
    - About traditional Indian games
        - Simple rules and inexpensive
        - Involve strategy making and a lot of physical exercise; quick and brisk movements
        - Demand physical fitness, strength, stamina, speed, endurance, flexibility, quick thinking
        - Issues

        1. Less popular - Even for other sports like football, many people watch European clubs play, but when Intercontinental Cup was held in Mumbai this year, Sunil Chettri had to appeal to fans to come watch the team play
        2. Currently only Kabaddi is included in international sporting events
        3. Chiefs of sports federations run the Federation as their personal fiefdom leading to corruption and deserving sportspersons being left out
        4. Despite below initiatives, financial and other incentives would only be given to players from select sports, probably Olympic, CWG and Asian Games sports
        5. Education tend to be higher priority for the average Indian household instead of extra-curricular activities, which are often considered a waste of time
    - Way forward
        1. Pro Kabaddi league (Gujarat Fortunegiants), Khelo India, Khelo India school games, Khel Mahakumbh by GJ govt
        2. Kabaddi already a sport in Asian Games
        3. Traditional sports need minimal infra and hence expenditure
        4. Khelo India aims at mainstreaming sport as a tool for individual development, community development, economic development and national development
        5. Movies like dangal, sultan, chak de changing perception about other games
- While working picked up playing foosball/table football
    - Each team of one or two human players controls four rows of foos-men, one row each for the goalkeeper, defenders, midfield and strikers
    - Table soccer was included in the recently held Delhi Olympic Games
    - Table configuration – 1 goalie, 2 defenders, 5 midfielders in the middle of the table, 3 attackers at front of the table

## Place related – Ahmedabad and Gujarat

- Population of 55 lakh
- History and culture
    - Most famous for Gandhiji's Sabarmati Ashram – Dandi march from here from 12 Mar 1930
    - In 2017, Old Ahmedabad/walled city (founded by Sultan Ahmed Shah) declared India's first UNESCO World Heritage City
        - Protected by international treaties
        - Govt will receive technical assistance from UNESCO in conservation
        - More revenue and forex due to rise in tourism
    - Sidi Saiyyed Mosque is famous for its intricately carved stone latticework windows (jali), which also inspired the logo of IIM-A
    - Famous architect B V Doshi has designed an underground cave like art gallery called Amdavad ni Gufa
    - Famous for kite festival during Uttarayan/Sankranti in Jan
    - Gujarati thali
    - Mrinalini Sarabhai established the Darpan Academy of Performing Arts
    - Adalaj step well
- Science
    - Vikram Sarabhai established the Physical Research Lab in 1947 and also helped set up eminent institutions like IIM A, CEPT (Centre for Environmental Planning and Tech) and ATIRA (Ahmedabad Textile Industry's research Association)

  - ISRO's Space Applications Centre also has a large campus in Ahmedabad
- Economy
  - Due to presence of several educational instis, Ahmedabad-Gandhinagar corridor has emerged as an technological and R&D hub
  - GIFT City – IT and Finance industry – aims to become new financial capital of the world
    - GJ International Finance Tech City
    - Numerous tax incentives for International Financial Services companies like lower Minimum Alternate Tax of 9% from 18.5%, no STT, no Commodity Txn Tax, no Dividend Distribution Tax, no LTCG, 10 years tax holiday
    - This year's Budget has a proposal that foreigners performing txns in derivatives, bonds, GDRs on a stock exchange located in GIFT shall not pay short term capital gains tax. Also, plans to set up a unified regulator for IFSC
    - An IFSC is thus a jurisdiction that provides world class financial services to non-residents and residents, to the extent permissible under the current regulations, in a currency other than the domestic currency (Indian rupee) of the location where the IFSC is located
  - Ahmedabad was once known as the Manchester of the East for its textile industry. Today India is the 2nd largest cotton textile centre in India after Mumbai
  - Largest supplier of denim and one of the largest exporters of gems and jewellery in the country – Arvind Mills is a big supplier of denim
  - It is also home to some of the biggest pharma companies of India – Zydus Cadilla and Torrent pharma
  - Chemical and agro and food processing industry also present – Amul
  - Tata Motors plant in Sanand to manufacture Nano
  - AMC was first municipality in India to have issued municipal bonds and enjoys a high credit rating
- Geography
  - Situated on the banks of Sabarmati
  - Sabarmati riverfront
- Economy of Gujarat
  - Agri – cotton, groundnuts, sugar cane, milk and milk products
  - Industrial – pharma, cement, textile, vegetable oil, chemicals, automobile, gems and jewellery, crude oil refining (refinery at Jamnagar is world's largest), Alang ship yard (world's largest ship breaking yard)
  - Vibrant Gujarat is biennial investors' summit by GoG. platform to understand and explore business opportunities in the State of Gujarat

# Job related

- What was your role?
  - As a Business Analyst, core function was data mapping. For this, had to understand own system, its functionalities and data requirements. Then had to look at data of upstream system and map relevant data from upstream system to mine
  - BAs also used to function as project managers and had to perform tasks like gathering requirements and coordinating with Compliance users, and coordinating development and testing teams
- What does AML team do? All about money laundering – what, how, why etc
  - set of procedures, laws and regulations designed to stop the practice of generating income through illegal actions

    - AML regulations require institutions issuing credit or allowing customers to open accounts to complete due-diligence procedures to ensure they are not aiding in money-laundering activities
    - Proceeds from trade of illegal goods, corruption of public funds, tax evasion, drug trafficking, human trafficking etc need to be laundered
        - One of the most common ways to launder money is to run it through a legitimate cash-based business owned by the criminal organization
        - Deposit cash in smaller increments
    - Most anti-money laundering laws openly conflate money laundering (which is concerned with source of funds) with terrorism financing (which is concerned with destination of funds) when regulating the financial system
    - Installs and monitors a suite of applications to detect and report potential Money Laundering activities – comprises of 3 solutions mainly – WLF, SAM and CDD
- How is money laundered
    - Structuring – cash broken down into smaller components and deposit those in various accounts – SAM gives a party + related party level view to check this
    - Cash intensive businesses like bars and restaurants
    - Dealing in art work where pricing is subjective and buyers and sellers' info secret
    - Round tripping – money sent to tax havens and brought back as FDI
    - Gambling
    - Bank capture
- Why is AML required
    - Bad for society – terrorists get funding to carry out terrorist activities, criminals get an advantage as they are able to convert black money into white and are encouraged to conduct their criminal activities
    - Particularly bad for India as a largest chunk of banking sector is with the public sector and when these banks are defrauded, indirectly it is the taxpayer who pays the price for it
    - Bad for the bank involved – hefty fines, for eg.
        - Last month RBI imposed a Rs. 3 crore fine on J&K bank and Deutsche Bank
        - Canara Bank fined $1.2 mn by UK regulator recently
        - Habib Bank, Pak fined $225 mn – last year
    - money accumulated illegally and with no regulation prevents capital from flowing into socioeconomically productive industries
    - The imbalance in money flow also inevitably leads to further printing of money, harming the purchasing power of a country's currency. If not controlled, this inflation can cripple and erode an economy
    - In cases of robbery, embezzlement or larceny, the enforcing agency can frequently return the funds or property uncovered during money-laundering investigations to the victims of the crime
- What projects did you work on? Explain.
    - In very first project, which was more of an enhancement, Compliance team had realized that RBI sends us a list of 14 Directors associated with entities in the Wilful Defaulters list. Since the main party in the watchlist was the entity, we used to screen all organizations having relationship with bank against this list, but did not screen persons against this list of Directors. My job was to modify the screening logic to load all these director names to the application database and then perform daily screening of persons in bank database against this list
- About flagship project : My first major project was implementing AML solutions for ABC project. It required implementation of 3 different solutions – one was watchlist screening in Real Time against only the Sanctions

lists while onboarding customers, next was daily watchlist screening of all of bank's customers against all relevant watchlists and last phase was the implementation of Customer Due Diligence module and streamlining the output of the first 2 systems to CDD module to arrive at an accurate risk profile of the customer

- USP : automation, streamlining alerts into CDD module
- Inputs into CDD – WLF alerts + High net worth + Industry + Occupation

- What is SAM(Suspicious Activity Monitoring)?
  - Burst in beneficiary/burst in originator over a period of 7 days
  - Deviation from past 6 months' history – compared with avg txn/month
  - Account dormant over last 6 or 12 months suddenly receiving money
  - Txn from high risk country, account or party
- What is SWIFT? How could PNB have prevented fraud?
  - About PNB fraud
    - fraudulent transactions totaling Rs.11,400 crore at Punjab National Bank's (PNB) Brady House branch in Mumbai
    - employees who willfully manipulated SWIFT, the electronic messaging system used for overseas funds transfer.
    - issuing letters of understanding (LoU) on behalf of companies associated with Nirav Modi, to avail credit from overseas branches of Indian banks
    - None of the aforementioned fraudulent transactions were registered on the bank's Core Banking Solution (CBS), thus enabling it to go unnoticed.
    - A letter of undertaking is a document issued by a bank, guaranteeing the credit-worthiness of a client for overseas export payments. The bank stands as guarantor for the client and is liable for the repayment of the principal and interest of the amount for which the LoU was drawn
  - About SWIFT
    - Society for Worldwide Interbank Financial Telecommunication
    - provides a network that enables financial institutions worldwide to send and receive information about financial transactions in a secure, standardized and reliable environment
    - SWIFT does not facilitate funds transfer: rather, it sends payment orders, which must be settled by correspondent accounts that the institutions have with each other. Each financial institution, to exchange banking transactions, must have a banking relationship by either being a bank or affiliating itself with one (or more) so as to enjoy those particular business features
  - This could have been prevented in XYZ bank because there these txns before leaving the bank used to come to my system for RT-WLF screening, then used to come back at the end of the day for batch screening in SAM
  - Although PNB mistake was not made by XYZ, catching fraudulent txns still depends on rules that have been activated in SAM and the thresholds prescribed in each of these rules
- About FATF
  - Intergovernmental org with headquarters in Paris, founded in 1989 on the initiative of G7 countries to develop policies to combat money laundering and terrorism financing
  - 38 members including India
  - Issued 40 (AML) + 9 (terrorist financing) recommendations
  - Monitors progress in implementation of FATF recommendations through peer reviews
  - FATF blacklist called Non-cooperative countries or territories
  - International Cooperation Review Group aka Grey List – Pak placed in this

- Regulators in other countries?
    - Hong Kong Monetary Authority
    - People's Bank of China
    - OJK for Indonesia
    - State Bank of Vietnam
    - Central Bank of Republic of China (Taiwan)
- RBI guidelines on KYC and AML
    - Guidelines are issued under Sec 35A of the Banking Regulation Act, 1949 and Rule 9(14) of Prevention of Money-Laundering Rules 2005 (ruled framed by Central Govt in consultation with RBI under PMLA and published in gazette by Dept of Revenue, Finance Ministry)
    - Section 51A of the Unlawful Activities (Prevention) Act, 1967 for prevention of, and for coping with terrorist activities. In terms of Section 51A, the Central Government is empowered to freeze, seize or attach funds and other financial assets or economic resources held by, on behalf of or at the direction of the individuals or entities listed in the Schedule
    - KYC guidelines have been revisited based on recommendations of FATF on AML standards and on Combating Financing of Terrorism
    - Objective is to prevent banks/FIs from being used, intentionally or unintentionally by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks/FIs to know/understand their customers and their financial dealings better and manage their risks prudently
    - Customer acceptance policy should be clearly defined so that
        - no account is opened in fictitious name
        - parameters of risk perception like nature of business activity, location of customer and his clients, mode of payments, volume of turnover, social and financial status are clearly defined
        - identity of customer should not match with any person or entity whose name appears in sanction lists circulated by RBI
    - CDD requirements while opening accounts – E-KYC of UIDAI is valid
    - If a customer does not possess required docs, he can be allowed to open a Small Account where total credit should be < 1 lakh per year, total withdrawals and transfers should be <10k per month and balance should be <50k
    - PEPs and RCAs - Banks should verify the identity of the person and seek information about the sources of funds before accepting the PEP as a customer. The decision to open an account for a PEP should be taken at a senior level which should be clearly spelt out in the bank's Customer Acceptance Policy. Banks should also subject such accounts to enhanced monitoring on an on-going basis. The above norms should also be applied to the accounts of the family members or close relatives of PEPs
    - CDD requirements : KYC exercise should be done at least every two years for high risk customers, every eight years for medium risk customers and every ten years for low risk customers
    - Partial freezing (disallow all debits) of accounts can be done by giving 3 month notice to customer to comply with KYC/AML requirements. After 6 months of partial freezing, completely freeze the account

  - In the circumstances when a bank/FI believes that it would no longer be satisfied about the true identity of the account holder, the bank/FI should file a Suspicious Transaction Report (STR) with Financial Intelligence Unit – India (FIU-IND) under Department of Revenue, Ministry of Finance
  - "Money Mules" can be used to launder the proceeds of fraud schemes (*e.g.,* phishing and identity theft) by criminals who gain illegal access to deposit accounts by recruiting third parties to act as "money mules". In order to minimise the operations of such mule accounts, banks should strictly adhere to the guidelines on opening of accounts and monitoring of transactions
  - Banks/FIs should exercise ongoing due diligence with respect to every customer and closely examine the transactions to ensure that they are consistent with the customer's profile and source of funds as per extant instructions
  - Banks/FIs should pay particular attention to the following types of transactions:
    - large and complex transactions, and those with unusual patterns, which have no apparent economic rationale or legitimate purpose.
    - transactions which exceed the thresholds prescribed for specific categories of accounts.
    - transactions involving large amounts of cash inconsistent with the normal and expected activity of the customer.
    - high account turnover inconsistent with the size of the balance maintained
  - Sanctions list – UN Al Qaeda Sanctions List and UN 1988 Sanctions List (Taliban)
- Improvement – If not already done, RBI could come up with more precise guidelines on tuning exercise performed by banks. Number of alerts to be generated is decided by the Compliance team, and since it also has to check the alerts, it creates an incentive to deliberately set parameters such that number of alerts is low

## RBI related

- Depts within RBI – Banking regulation, non-banking regulation, cooperative bank regulation, currency mgt, forex mgt, monetary policy, govt and bank accounts, payment and settlement systems, financial inclusion and development, consumer education and protection, economic and policy research
- A central bank performs several important functions for the economy: it controls the money supply; sets the rate of interest on borrowing and lending money; manages the external sector including the exchange rate; supervises and regulates the financial sector, notably banks; it often regulates credit and foreign exchange markets; and, seeks to ensure financial stability, domestic as well as on the external front
- Its tasks being somewhat complex and technical, central banks are ideally headed and manned by technocrats or field experts – typically economists, academics, commercial bankers, and occasionally private sector representatives, appointed by the government but not elected to the office
- Roles played by RBI
  - Monetary Authority : keeping inflation under check and ensuring adequate supply of liquidity
  - Prescribes regulations for sound functioning of banks and financial institutions, including NBFCs;
  - Issuer of Currency
  - Manager of Foreign Exchange : Formulates policies to facilitate external trade and payments, facilitates foreign investments in India and Indian investments abroad
  - Banker to the Government : merchant banking function for governments; Encourages development and orderly functioning of Government securities market
  - Payment Systems : establishment of robust, efficient, secure payment and settlement system

- Bankers' Bank : Performs lender of the last resort function
- Developmental Role
- Research

# Current affairs and issues related

## RBI tussle with govt

- Reasons
    - Govt insisting RBI stick to Basel norms on capital adequacy so that banks can lend more
        - The Board, while deciding to retain the CRAR at 9%, agreed to extend the transition period for implementing the last tranche of 0.625% under the Capital Conservation Buffer (CCB), by one year, i.e., up to March 31, 2020
    - Govt seeking relaxation in PCA norms allowing banks to lend more
        - banks under PCA, it was decided that the matter will be examined by the Board for Financial Supervision (BFS) of RBI
        - Board also advised that the RBI should consider a scheme for restructuring of stressed standard assets of MSME borrowers with aggregate credit facilities of up to ₹ 250 million, subject to such conditions as are necessary for ensuring financial stability
    - Govt insisting that NBFCs are facing liquidity crunch and RBI should step in to resolve this
    - Govt eyeing RBI's reserves
        - Board decided to constitute an expert committee to examine the Economic Capital Framework of the RBI, the membership and terms of reference of which will be jointly determined by the Government of India and the RBI
        - This is wrong because it weakens the balance sheet of the central bank and provides the wrong incentive to the govt as it weakens the incentive to control expansion of spending
- Governments have sparred with the RBI before on the issue of autonomy, but the NDA government went one step further by starting consultations under Section 7 of the RBI Act, which gives the Centre the power to direct the RBI to act in specific ways
- This was not a right measure since RBI's autonomy is crucial in public interest because
    - Govt's horizon of decision making is short term as there are always upcoming elections of some sort and govt needs to resort to populist alternatives where manifestos have not been delivered upon. by virtue of being nominated rather than elected, central bankers have horizons of decision-making that tend to be longer than that of governments, spanning election cycles. by their mandate central banks are committed to stabilise the economy over business and financial cycles, and hence, have to peer into the medium to long term. Unsurprisingly, central banks strive to build credibility through a series of difficult choices that reflect sacrificing short-term gains for long-term outcomes such as price or financial stability
    - PSBs constitute a major portion of India's banking system. PSBs are owned by govt and regulated by RBI. If govt has influence over RBI, there will be a conflict of interest
    - Govt spends money, especially so before elections, which tends to increase inflation. Inflation erodes the value of savings of common man and hence RBI, as the monetary authority, has been given the legal mandate of keeping inflation at 4 +-2%
    - Relaxation in bank capital requirements can lead to greater credit creation but also leads to increased lending to sub-prime assets and can result in financial crisis

- Allowing foreign capital to flood into the economy can temporarily ease financing pressures of the govt but a sudden stop or exodus of this capital can trigger a collapse of exchange rate
- How is RBI's autonomy eroded
  - Appointing govt or govt affiliated officials to senior mgt rather than technocrats
  - Eroding statutory powers of the central bank
  - Favouring discretionary or joint decision making with direct govt interventions
  - Setting up parallel regulatory agencies with weaker statutory powers
- Although govt being the representatives of the people have been given the power to override RBI, this power is meant to be used only in exceptional circumstances, say when RBI takes a drastic step when it is not called for or when RBI takes an irrational step. In that case, to bring back normalcy, it is ok for govt to impose Sec 7. But in a business as usual scenario, and especially when steps like PCA have been taken for the benefit of the banking sector, it was not right to make such a threat
- Regulation of PSBs – RBI is statutorily limited in undertaking the full scope of actions against public sector banks (PSBs) – such as asset divestiture, replacement of management and Board, license revocation, and resolution actions such as mergers or sales — all of which it can and does deploy effectively in case of private banks

## IL&FS issue? Why did it cause liquidity crunch in NBFCs?

- What
  - L&FS Ltd, or Infrastructure Leasing & Finance Services, is a core investment company and serves as the holding company of the IL&FS Group – LIC largest shareholder with 25.34%
  - Defaulted in payment obligations of bank loans and failed to meet commercial paper redemption obligations and also defaulted on inter-corporate deposits
  - Debt to equity ratio of 18.7(should ideally be 2), total debt of about Rs. 91k crore
  - Due to IL&FS crisis, banks reluctant to lend to NBFCs
- Solutions
  - NCLT granted permission to the Centre to take over the board of IL&FS
  - NCLT appointed a 6 member panel to take over the mgt of IL&FS with immediate effect – panel headed by Uday Kotak
  - RBI allowed banks to provide Partial Credit Enhancement to bonds issued by systemically important non-deposit taking NBFCs registered with RBI and Housing FCs registered with NHB
  - RBI injected liquidity in the system through a series of OMOs
  - Banks can use g-secs as level 1 high quality liquid asset equivalent to their incremental lending to NBFCs and HFCs
  - Capital funds lending limit for banks to a single non-infra NBFC has been hiked to 15% from earlier 10%

## Payments and Settlement Systems Act 2007 proposed amendments – dissent note

- Payment systems are a sub-set of currency which is regulated by the RBI.
- The overarching impact of Monetary policy on payment and settlement systems and vice versa provides support for regulation of payment systems to be with the monetary authority
- There is an underlying bank account for payment systems which is under the purview of banking system regulation which is vested with the RBI.
- Settlement systems are finally posted in the books of account of banks with the RBI to attain settlement finality. Regulating these entities goes hand in hand with the settlement function
- In India, the payment system is bank-dominated. Regulation of the banking systems and payment system by the same regulator provides synergy and inspires public confidence in the payment instruments

- Regulation of the Payment System by the Central Bank is the dominant international model for stability consideration

## IBC, 2016

- Bankruptcy Law Reforms Committee was headed by T K Vishwanathan
- comprehensive insolvency legislation encompassing all companies, partnerships and individuals (other than financial firms)
- Corporate debtors – 2 stage process : Insolvency Resolution Process and Liquidaton
    - Creditor initiates IRP against a corporate debtor at the NCLT (defaulting debtor can also initiate)
    - NCLT orders a moratorium on the debtor's operations for the period of the IRP
    - NCLT appoints an insolvency professional or 'Resolution Professional' to administer the IRP. The Resolution Professional's primary function is to take over the management of the corporate borrower and operate its business as a going concern under the broad directions of a committee of creditors
    - Creditors committee constituted by the IP
    - Each decision of the creditors committee requires a 75% majority vote. Decisions of the creditors committee are binding on the corporate debtor and all its creditors
    - The creditors committee considers proposals for the revival of the debtor and must decide whether to proceed with a revival plan or liquidation within a period of 180 days (subject to a one-time extension by 90 days)
    - If RP not approved within 180(+90) days or 75% majority of creditor's committee votes for liquidation or NCLT rejects the RP – liquidation
    - NCLT passes an order for liquidation
    - After the costs of insolvency resolution (including any interim finance), secured debt together with workmen dues for the preceding 24 months rank highest in priority. Central and state Government dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors
- Individual/Unlimited partnerships
    - two distinct processes in case of insolvencies: automatic fresh start and insolvency resolution
    - Under the automatic fresh start process, eligible debtors (basis gross income) can apply to the Debt Recovery Tribunal (**DRT**) for discharge from certain debts not exceeding a specified threshold, allowing them to start afresh
    - The insolvency resolution process consists of preparation of a repayment plan by the debtor, for approval of creditors. If approved, the DRT passes an order binding the debtor and creditors to the repayment plan. If the plan is rejected or fails, the debtor or creditors may apply for a bankruptcy order
- Creditor driven insolvency process
- Institutional infra
    - Insolvency and Bankruptcy Board of India as the Insolvency Regulator whose functions include (i) overseeing the functioning of insolvency intermediaries i.e., insolvency professionals, insolvency professional agencies and information utilities; and (ii) regulating the insolvency process.
    - Insolvency Resolution Professionals : class of regulated but private professionals having minimum standards of professional and ethical conduct; verifies the claims of the creditors, constitutes a creditors committee, runs the debtor's business during the moratorium period and helps the creditors in reaching a consensus for a revival plan. In liquidation, the insolvency professional acts as a liquidator and bankruptcy trustee

    - Information Utilities : to collect, collate, authenticate and disseminate financial information of debtors in centralised electronic databases. The Code requires creditors to provide financial information of debtors to multiple utilities on an ongoing basis. Such information would be available to creditors, resolution professionals, liquidators and other stakeholders in insolvency and bankruptcy proceedings
    - Adjudicatory authorities : NCLT and DRT; appeals against their decisions lie with NCLAT and DRAT and then with SC
- Why IBC, 2016
    - Earlier there were several laws that dealt with insolvency for companies, such as the Sick Industrial Companies Act, the Recovery of Debt Due to Banks and Financial Institutions Act, and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI)
    - investable money locked for a long time in litigations is the least preferred situation for business partners and lender
    - bank unable to loan out more due to provisioning requirements
    - companies unable to access new loans
    - will help to ensure confidence of banks, foreign investors, associated companies in crisis mitigation mechanism related to business entities in the country
    - An early resolution with sound principles will help the related parties like banks not to suffer from the failure of the business entity

## Rupee depreciation

- Rise in crude oil prices
- Widening trade deficit
- US-China trade war means that outlook for Indian exports does not look very bright
- Turkey lira crisis – investors club both countries into the emerging markets section in investment models. So when investors get rid of Lira, they get rid of the Rupee too
    - Turkish Lira has depreciated a lot this year against USD owing to
        - the country's deteriorating ties with the US (trade war) and other western nations which are sources of capital inflows into Turkey
        - Turkish President's increasing authoritarianism leading to quelling of free and factual reporting by financial analysts and intervention in Turkey's central bank's functioning
        - political instability
        - high current account deficit
    - High inflation
- Interest rates in the US are rising, which is affecting capital flows to emerging markets
- RBI policy
    - it only intervenes to reduce volatility and does not target any particular level
    - Not allowing exchange rate to adjust on the downside will only increase the dependence on foreign debt
- Pros
    - Gradually depreciating rupee would help India as imports would go down and exports become more competitive in the international markets
- Cons
    - Costlier imports
    - Higher interest costs for companies that have borrowed from abroad

## Resolution of stressed assets – revised framework (12th Feb 2018)

- Before revised framework
  - Asset Quality Review report by RBI that indicated that PSBs had higher NPAs than reported
  - Joint Lenders' Forum – at least 75% creditors by value and 60% by numbers had to agree to the restructuring plan
  - Strategic Debt Restructuring plan – banks got right to convert full or part of their loans into equity shares
  - S4A (Scheme for Sustainable Structuring of Stressed Assets) – envisages determination of the sustainable debt level for a stressed borrower, and bifurcation of the outstanding debt into sustainable debt and equity/quasi-equity instruments which are expected to provide upside to the lenders when the borrower turns around
- After revised framework
  - Lenders shall identify incipient stress in loan accounts, immediately on default, by classifying stressed assets as special mention accounts (SMA) as per the following categories : SMA 0 for payment due between 0-30 days, SMA 1 for dues between 31-60 days, SMA 2 for dues between 61-90 days
  - lenders shall report credit information, including classification of an account as SMA to Central Repository of Information on Large Credits (CRILC) on all borrower entities having aggregate exposure of ₹ 5 crore and above with them – defaults to be reported on weekly basis
  - All lenders must put in place Board-approved policies for resolution of stressed assets under this framework, including the timelines for resolution – called Resolution Plan
  - As soon as there is a default in the borrower entity's account with any lender, all lenders − singly or jointly − shall initiate steps to cure the default. The resolution plan (RP) may involve any actions / plans / reorganization including, but not limited to, regularisation of the account by payment of all over dues by the borrower entity, sale of the exposures to other entities / investors, change in ownership, or restructuring
  - RPs involving restructuring / change in ownership in respect of 'large' accounts (i.e., accounts where the aggregate exposure of lenders is ₹ 100 crore and above), shall require independent credit evaluation (ICE) of the residual debt5 by credit rating agencies. For accounts over 500 crore, 2 ICEs required
  - For large accounts of Rs. 2000 crore+, RP to be implemented within 180 days. If not implemented, lenders to file insolvency application under IBC within 15 days
  - In case of restructuring, the accounts classified as 'standard' shall be immediately downgraded as non-performing assets (NPAs), i.e., 'sub-standard'
  - Borrowers who have committed frauds/ malfeasance/ wilful default will remain ineligible for restructuring
- capital should be understood as the "own funds" used to create assets by banks, as against borrowed funds like deposits. The capital maintained by the bank merely shows the proportion of own funds brought in by the bank in the total funds deployed towards creating assets. There is a misconception that capital is a pile of money stacked away as some sort of "rainy-day fund", and that the economy is deprived of that pile of money. The reality couldn't be farther from the truth – the capital maintained by banks would have already been deployed on its balance sheet towards creating assets, including loans

## PCA framework

- PCA framework was introduced in December 2002 as a structured early intervention mechanism designed to help banks regain health by preserving capital.
- Revised PCA Framework was issued by the Reserve Bank on April 13, 2017

- PCA can thus be seen as first, stabilizing the banks at risk, and then, undertaking the deeper bank reforms needed for long-term viability of the business model of these banks
- Indicators to be tracked for Capital, asset quality and profitability would be CRAR/ Common Equity Tier I ratio1, Net NPA ratio2 and Return on Assets respectively
- Leverage would be monitored additionally as part of the PCA framework
- Breach of any risk threshold (as detailed under) would result in invocation of PCA
- Currently Capital Conservation Buffer is 1.875%, addition of 0.625% delayed to 2020
- Min CET 1 capital ratio is 5.5%
- Min Tier 1 capital ratio is 7%
- Min Total capital ratio is 9%
- Based on tracked indicators crossing certain defined thresholds, banks are put under PCA and restrictions are imposed upon them for example
    - Upon crossing risk threshold 1, there is a restriction on dividend distribution/remittance of profits and promoters are required to bring in additional capital
    - Upon crossing risk threshold 2, in addition to above, there is restriction on branch expansion and higher provisions are required
    - Upon crossing risk threshold 3, in addition to above, restriction imposed on management compensation

## Basel norms

- Basel rules are an internationally accepted regulatory framework providing minimum standards to be met by banks
- Basel II norms hinged on three pillars – capital adequacy, supervisory review, and market discipline. In particular, capital charges were to be made for credit risk, market risk and operational risk that banks faced.
- Basel III norms
    - stricter requirements for the quality and quantity of regulatory capital, in particular reinforcing the central role of common equity;
    - an additional layer of common equity - the capital conservation buffer - that, when breached, restricts discretionary pay-outs to help meet the minimum common equity requirement;
    - a countercyclical capital buffer, which places restrictions on participation by banks in system-wide credit booms with the aim of reducing their losses in credit busts;
    - a leverage ratio - a minimum amount of loss-absorbing capital relative to all of a bank's assets and off-balance sheet exposures regardless of risk weighting;
    - liquidity requirements - a minimum liquidity ratio, the Liquidity Coverage Ratio (LCR), intended to provide enough cash to cover funding needs over a 30-day period of stress; and a longer-term ratio, the Net Stable Funding Ratio (NSFR), intended to address maturity mismatches over the entire balance sheet; and
    - additional requirements for systemically important banks, including additional loss absorbency and strengthened arrangements for cross-border supervision and resolution
- Under Basel III norms, unexpected losses are a function of the cumulative default rates (CDR) observed in the credit ratings provided by the credit rating agencies (CRAs). The CDR is nothing but the probability of a non-default rating assigned by a CRA turning into a default rating within a certain period of time. Based on internationally observed CDRs and recovery rates, Basel norms have prescribed risk weights for various credit exposures. However, the CDRs and the loss given default observed in India are much higher than that observed internationally. With this kind of default behaviour, applying the Basel specified risk weights would understate

the true riskiness in the loan assets carried on the books of Indian banks. As the need for repeated recapitalisation has proved, banks in India need to aspire to have higher capital levels.

- Provisions (made from current earnings) are to cover expected losses while level of capital maintained by the bankl is for covering unexpected losses. If banks don't have adequate capital, losses erode into deposits. Banks have to maintain adequate capital to ensure that the probability of deposits being eroded is close to zero

## Latest circulars

- decided by the Government of India to increase w.e.f. November 02, 2018 Interest Equalisation rate from 3% to 5% in respect of exports by the Micro, Small & Medium Enterprises (MSME) sector manufacturers under the Interest Equalisation Scheme on Pre and Post Shipment Rupee Export Credit.
- RBI has decided to conduct purchase of Government securities under Open Market Operations (OMOs) for an aggregate amount of ₹ 400 billion in the month of December 2018
- govt announced a Rs. 2.1 lakh crore recapitalization plan for PSBs – 80k crore through recap bonds, 8k crore as budgetary support (total 1.5 lakh crore from govt capital infusion)
- Latest MPC : keep the policy repo rate under the liquidity adjustment facility (LAF) unchanged at 6.5 per cent
- Speeches
    - Capital Account Convertibility by G Padmanabhan in 2015
    - PCA framework by Viral Acharya
    - Banking regulator independence from govt by Viral Acharya
    - Banking regulatory powers should be ownership neutral by Urjit Patel

# India's banking sector related

- Capital Account Convertibility
    - Capital account convertibility means the freedom to convert rupees into foreign currency and back for capital transactions. India has current account convertibility but not capital account convertibility.
    - Macro-economic parameters have to be stable before it is implemented
        - The low current account deficit should be sustained
        - fiscal deficit needs to be contained
        - The rupee as a currency should be more frequently traded internationally
    - Leads to free exchange of currency at lower rates and an unrestricted mobility of capital
    - Beneficial for a country because inflow of foreign investment increases, allowing companies to borrow at lower costs and fuelling growth
    - The flip side, though, is that it could destabilize an economy due to massive capital flows in and out of the country
- History of India's banking sector?
    - In 1969 the Indian government nationalised 14 major private banks
    - In 1980, 6 more private banks were nationalized
    - Regional Rural Banks (RRBs) also known as Gramin banks, are Indian scheduled banks (Government banks) operating at regional level in different States of India. They have been created with a view of serving primarily the rural areas of India with basic banking and financial services
    - The short-term co-operative credit structure operates with a three-tier system - Primary Agricultural Credit Societies (PACS) at the village level, Central Cooperative Banks (CCBs) at the district level and State Cooperative Banks (StCBs) at the State level.

    - PACS are outside the purview of the Banking Regulation Act, 1949 and hence not regulated by the Reserve Bank of India. StCBs/DCCBs are registered under the provisions of State Cooperative Societies Act of the State concerned and are regulated by the Reserve Bank. Powers have been delegated to National Bank for Agricultural and Rural Development (NABARD) under Sec 35 A of the Banking Regulation Act (As Applicable to Cooperative Societies) to conduct inspection of State and Central Cooperative Banks.
    - Primary Cooperative Banks (PCBs), also referred to as Urban Cooperative Banks (UCBs), cater to the financial needs of customers in urban and semi-urban areas
- NRE vs NRO account?
- CPI, WPI, IIP
- Data from RBI doc from mains prep – critical parameters like NPAs, CAD, fiscal deficit etc
    - CAD has ballooned to 2.9% of GDP in Q2(July-Sept) of this financial year – USD 19.1bn as compared to USD 6.9bn last year
        - Due to high trade deficit of USD 50bn (half of this is due to petroleum, oil and lubricants)
        - 26% of our import is of oil
    - FDI fell to USD 7.9bn in Q2 this year as against USD 12.4bn
    - FPI recorded net outflow of USD 1.6bn as against inflow of USD 2.1bn last year
    - Inflation was 3.3% in Oct (CPI was 140.6)
    - The Reserve Bank currently has Rs 9.79 lakh crore in reserves - a sum equivalent to 28 per cent of its assets – transferred 50k crore to govt as
    - Singapore banking system's overall NPL ratio decreased from 2.1% in Q3 last year to 1.9% this year – local banks NPL ratio was 1.5%
    - Forex reserves are around 393 bn USD
    - GDP growth rate was 6.7% last year as per RBI annual report; expected to rise to 7.4% this financial year
- GST
- FRBM Act 2003
    - Act of the Parliament of India to institutionalize financial discipline, reduce India's fiscal deficit, improve macroeconomic management and the overall management of the public funds
    - main purpose was to eliminate revenue deficit
    - aim was to bring down fiscal deficit to 3% by 2008
    - FRBM review committee – debt to GDP ratio of 60% should be targeted, fiscal deficit of 3% to be targeted