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ORIGINAL ARTICLE

Financial Sector Reforms in India: An Analysis

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ABSTRACT

Indian banking system operated for a long time with high reserve requirements both in the form of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR). This was mainly to accommodate the high fiscal deficit and its monetisation. The efforts in the recent period have been to lower both the CRR and SLR. The SLR has been gradually reduced from a peak of 38.5 per cent to 25 per cent. The CRR was reduced from its peak level of 15.0 per cent maintained during 1989 to 1992 to 4.5 per cent of NDTL in June 2003. Although the Reserve Bank continues to pursue its medium-term objective of reducing the CRR, in recent years, on a review of macroeconomic and monetary conditions, the CRR has been revised upwards to 6.0 per cent (to be effective from March 3, 2007). The banking industry has the potential and the ability to rise to the occasion as demonstrated by the rapid pace of automation which has already had a profound impact on raising the standard of banking services. The financial strength of individual banks, which are major participants in the financial system, is the first line of defence against financial risks.

Key words: *Analysis, Finence Sectors, Economy*

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Introduction

Finance and growth are intimately interlinked. As the economy growth and becomes more sophisticated, the banking sector has to develop pari passu in a manner that it supports and stimulates such growth with increasing global integration, the Indian baking system and financial system has had to be as a whole strengthened so as to be able to compete. India has had more than a decade of financial sector reforms during which there has been substantial transformation and liberalization of the whole financial system. It is, therefore, an appropriate time to take stock and assess the efficiency of our approach. It is useful to evaluate how the financial system has performed in an objective quantitative manner. This is important because India's path of reforms has been different from most other emerging market economics. It has been a measured, gradual, cautious, and steady process, devoid of many flourishes that could be observed in other counties.

OBJECTIVE OF THE STUDY

The present paper deal with the financial sector reforms in India, impact of financial sector reforms in India and future challenges for Indian banks. The paper raises some issues for the future of this sector.

FINANCIAL SECTOR REFORMS IN INDIA

The deregulation of interest rates constituted an integral part of financial sector reforms. The interest rate regime has been largely deregulated with a view to achieving better price discovery and efficient resource allocation. Banks now have flexibility to decide their deposit and lending rate structures and manage their assets and liabilities accordingly. At present, apart from interest rates on savings deposits and NRI deposits on the deposit side, and export credit and small loans up to Rs. 2 lakh on the lending side, all other interest rates have been deregulated.

It has been the endeavor of the Reserve Bank to establish an enabling regulatory framework with prompt and effective supervision, and development of legal, technological and institutional infrastructure. Persistent efforts, therefore, have been made towards adoption of international benchmarks, as appropriate to Indian conditions. In 1994, a Board for Financial Supervision (BFS) was constituted comprising select members of the Reserve Bank Board with a variety of professional expertise to exercise 'undivided attention to supervision' and ensure an integrated approach to supervision of commercial banks and financial institutions. The Reserve Bank had instituted a state of-the-art Off-site Monitoring and Surveillance (OSMOS) system for banks in 1995 as part of crisis management framework for Early Warning System (EWS) and as a trigger for on-site inspections of vulnerable institutions.

The scope and coverage of off-site surveillance has since been widened to capture various facets of efficiency and risk management of banks. As a part of the financial sector reforms, the regulatory norms with respect to capital adequacy, income recognition, asset classification and provisioning have progressively moved towards convergence with the international best practices. These measures have enhanced transparency of the balance sheet of the banks and infused accountability in their functioning. Besides sub-standard assets, provisioning has also been introduced for the standard assets. Measures to reduce the levels of NPAs concentrated on improved risk management practices and greater recovery efforts facilitated by the enactment of Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002. Several other channels of NPA management have also been instituted, including Debt Recovery Tribunals, *Lok Adalats* (People's court) and corporate debt restructuring mechanism with separate schemes for small and medium industries.

The minimum capital to risk assets ratio (CRAR), which was earlier stipulated at eight per cent was revised to 9 per cent in 1999, which is one percentage point above the international norm. As some banks in the public sector were not able to comply with the CRAR stipulations, there was a need to recapitalise them to augment their capital base. Banks were allowed to raise capital from the market. In line with the amendment to incorporate market risk in Basel I, separate capital charge for market risk was also introduced in 2004. Accounting standards and disclosure norms were strengthened with a view to improving governance and bringing them in alignment with the international norms. The disclosure requirements broadly covered capital adequacy, asset quality, maturity distribution of select items of assets and liabilities, profitability, country risk exposure, risk exposures in derivatives, segment reporting, and related party disclosures. In April 2005, commercial banks were advised to put in place business continuity measures, including a robust information risk management system within a fixed time frame.

In view of the increasing degree of deregulation and exposure of banks to various types of risks, the Reserve Bank initiated measures for further strengthening and fine-tuning risk management systems in banks. The guidelines on asset-liability management and risk management systems in banks were issued in 1999 and Guidance Notes on Credit Risk Management and Market Risk Management in October 2002 and the Guidance Note on Operational risk management in 2005. In the Reserve Bank, the risk-based approach to supervision has been adopted since 2003 and about 23 banks have been brought under the fold of risk-based supervision (RBS) on a pilot basis. On the basis of the feedback received from the pilot project, the RBS framework is being reviewed.

As part of the reform programme, due consideration has been given to diversification of ownership of banking institutions for greater market accountability and improved efficiency. The public sector banks expanded their capital base by accessing the capital market, which diluted the Government ownership. To provide banks with additional options for raising capital funds with a view to enabling smooth transition to the Basel II, the Reserve Bank in January 2006, allowed banks to augment their capital funds by issue of additional instruments. With a view to enhancing efficiency and productivity through competition, guidelines were laid down for establishment of new banks in the private sector and the foreign banks have been allowed more liberal entry. Since 1993, 12 new private sector banks have been set up. As a major step towards enhancing competition in the banking sector, foreign direct investment in the private sector banks is now allowed up to 74 per cent, subject to conformity with the guidelines issued from time to time. The regulatory framework in India, in addition to prescribing prudential guidelines and encouraging market discipline, is increasingly focusing on ensuring good governance through "fit and proper" owners, directors and senior managers of the banks.

Transfer of shareholding of five per cent and above requires acknowledgement from the Reserve Bank and such significant shareholders are required to meet rigorous 'fit and proper' requirements. Banks have also been asked to ensure that the nominated and elected directors are screened by a nomination committee to satisfy 'fit and proper' criteria. Directors are also required to sign a covenant indicating their roles and responsibilities. The Reserve Bank has issued detailed guidelines on ownership and governance in private sector banks emphasizing diversified ownership. The Reserve Bank released a roadmap for foreign banks articulating a liberalised policy consistent with the WTO commitments in March 2005. The roadmap is divided into two phases. During the first phase, between March 2005 and March 2009, foreign banks wishing to establish presence in India for the first time could either choose to operate through branches or set up 100 per cent wholly owned subsidiaries (WOS), following the one-mode presence criterion. For new and existing foreign banks, it is proposed to go beyond the existing WTO commitment of 12 branches in a year.

During this phase, permission for acquisition of shareholding in Indian private sector banks by eligible foreign banks will be limited to banks identified by the Reserve Bank for restructuring. The second phase is scheduled to commence from April 2009 after a review of the experience gained and after due consultation with all the stakeholders in the banking sector. In this phase, three interconnected issues would be taken up. First, rules for the removal of limitations on the operations of the WOS and treating them at par with domestic banks, to the extent appropriate, would be designed and implemented. Second, the WOS of foreign banks, on completion of a minimum prescribed period of operation, may be allowed to list and dilute their stake so that, consistent with the guidelines issued on March 5, 2004, at least 26 per cent of the paid-up capital of the subsidiary is held by resident Indians at all times. Third, during this phase, foreign banks may be permitted to enter into merger and acquisition transactions with any private sector bank in India, subject to the overall investment limit of 74 per cent.

In recent years, comprehensive credit information, which provides details pertaining to credit facilities already availed of by a borrower as well as his payment track record, has become critical. Accordingly, a scheme for disclosure of information regarding defaulting borrowers of banks and financial institutions was introduced. In order to facilitate sharing of information related to credit matters, a Credit Information Bureau (India) Limited (CIBIL) was set up in 2000. The Banking Ombudsman Scheme was notified by the Reserve Bank in 1995 to provide for a system of redressal of grievances against banks. The scheme sought to establish a system of expeditious and inexpensive resolution of customer complaints. The scheme was revised twice, first in 2002 and then in 2006. At present, the scheme is being executed by Banking Ombudsman (BO) appointed by the Reserve Bank at 15 centres covering the entire country. The BO scheme covers all commercial banks and scheduled primary cooperative banks. The scheme was revised recently which brought more grounds of complaints within its ambit.

An independent Banking Codes and Standards Board of India was set up on the model of the UK in order to ensure that comprehensive code of conduct for fair treatment of customers is evolved and adhered to. With a view to achieving greater financial inclusion, since November 2005, all banks need to make available a basic banking 'no frills' account either with 'nil' or very low minimum balances as well as charges that would make such accounts accessible to vast sections of population. Banks were urged to review their existing practices to align them with the objective of 'financial inclusion'. The smooth functioning of the payment and settlement system is a pre-requisite for financial stability. The Reserve Bank, therefore, has taken several measures from time to time to develop the payment and settlement system in the country along sound lines. The Board for Regulation and Supervision of Payment and Settlement Systems (BPSS), set up in March 2005 as a committee of the Central Board of the Reserve Bank, is the apex body for giving policy direction in the area of payment and settlement systems.

Real time gross settlement (RTGS) was operationalised on March 26, 2004. Its usage for transfer of funds, especially for large values and for systemically important purposes, has increased since then. With introduction of RTGS, whereby a final settlement of individual inter-bank fund transfers is effected on a gross real time basis during the processing day, a major source of systemic risk in the financial system has been reduced substantially. A risk free payments and settlements system in government securities and foreign exchange was established by the Clearing Corporation of India Limited (CCIL), which is set up by banks. CCIL acts as the central counter party (CCP) for all the transactions and guarantees both the securities and funds legs of the transaction. Under the DvPIII mode of settlement that has been adopted, both the securities leg and the fund leg are settled on a net basis. The settlement through CCIL has thus reduced the gross dollar requirement by more than 90 per cent. A screen-based negotiated quote-driven system for dealings in the call/notice and the term money market (NDS-CALL) has been launched by the CCIL in September 18, 2006. The introduction of NDS-CALL helps in enhancing transparency, improving price discovery and strengthening market microstructure.

IMPACT OF FINANCIAL SECTOR REFORMS IN INDIA

Banks have been accorded greater discretion in sourcing and utilisation of resources, *albeit* in an increasingly competitive environment. The outreach of the Indian banking system has increased in terms of expansion of branches/ATMs. In the post-reform period, assets/liabilities of banks have grown consistently at a high rate. The financial performance of banks also improved as reflected in their increased profitability. Net profit to assets ratio improved from 0.49 per cent in 2000-01 to 1.13 per cent in 2003-04. Although it subsequently declined to 0.88 per cent in 2005-06, it was still significantly higher than that in the early 1990s. Banks have been successful in weathering the impact of upturn in interest rate cycle through increasing diversification of their income. Though banks had to incur huge expenditures on upgradation of information technology, the restructuring of the workforce in public sector banks helped them cut down the staff cost and increase in business per employee. Another welcome development has been the sharp reduction in non-performing loans (NPLs). Both gross and net NPLs started to decline in absolute terms since 2002-03. Gross NPLs as percentage of gross advances, which were above 15 per cent in the early 1990s, are now less than 3 per cent. This distinct improvement in asset quality may be attributed to the improved recovery climate underpinned by strong macroeconomic performance as well as several institutional measures initiated by the Reserve Bank/ Government such as debt recovery tribunals, *Lok Adalats*, scheme of corporate debt restructuring in 2001, the SARFAESI Act in 2002.

Since 1995-96, the banking sector, on the whole, has been consistently maintaining CRAR well above the minimum stipulated norm.

The overall CRAR for scheduled commercial banks increased from 8.7 per cent at end-March 1996 to 12.3 per cent at end-March 2006. The number of banks not complying with the minimum CRAR also declined from 13 at end-March 1996 to just two by end-March 2006. Improved capital position stemmed largely from the improvement in profitability and raising of capital from the market, though in the initial stages the Government had to provide funds to recapitalise weak public sector banks. Even though public sector banks continue to dominate the Indian banking system, accounting for nearly three-fourths of total assets and income, the increasing competition in the banking system has led to a falling share of public sector banks, and increasing share of the new private sector banks, which were set up around mid-1990s. It is clear that we are at the beginning of this new phase in the Indian banking with competitive pressure, both domestic and external, catching up and the need for banks to continuously reassess and reposition themselves in their business plans.

PERFORMANCE OF THE FINANCIAL SECTOR UNDER THE REFORM PROCESS

Banking sector reform has established a competitive system driven by market forces. The process, however, has not resulted in disregard of social objectives such as maintenance of the wide reach of the banking system or channelisation of credit towards disadvantaged but socially important sectors. At the same time, the reform period experienced strong balance sheet growth of the banks in an environment of operational flexibility. A key achievement of the banking sector reform has been the sharp improvement in the financial health of banks, reflected in significant improvement in capital adequacy and improved asset quality. This has been achieved despite convergence of the prudential norms with the international best practices. There have also been substantial improvements in the competitiveness of the Indian banking sector reflected in the changing composition of assets and liabilities of the banking sector across bank groups. In line with increased competitiveness, there has been improvement in efficiency of the banking system reflected inter alia in the reduction in interest spread, operating expenditure and cost of intermediation in general. Contemporaneously there have been improvements in other areas as well including technological deepening and flexible human resource management. A more detailed discussion on the performance analysis of the banking sector under the reform process is given below.

SOCIAL OBJECTIVES AND BALANCE SHEET MANAGEMENT

The Indian banking system has acquired a wide reach, judged in terms of expansion of branches and the growth of credit and deposits (Tables 1). The expansion of branch network peaked in the phase of social banking during the 1970s and 1980s.

Table 1: Progress of Commercial Banking in India

S. No.	Indicators	June 1969	June 1980	March 1991	March 1995	March 2000	March 2003
1	No of commercial banks	73	154	272	284	298	292
2	No of bank offices of which	8262	34594	60570	34234	67868	68561
	Rural and semi-urban bank offices	5172	23227	46550	46602	47693	47496
3	Population per office('000s)	64	16	14	15	15	16
4	Per capita deposit (Rs)	88	738	2368	4242	8542	12253
5	Per capita credit (Rs)	68	457	1434	2320	4555	7275
6	Priority sector advances@ (per cent)	15.0	37.0	39.2	33.7	35.4	33.7*
7	Deposits (per cent of national income)	15.5	36.0	48.1	48.0	53.5	51.8

@: Share of priority sector advances in total non-food credit of scheduled commercial bank; *: As at end March 2002.
Source: Reserve Bank of India.

Despite the slowdown in branch expansion since the 1990s, the population per bank branch, however, has not changed much since the 1980s, and has remained at around 15,000. It is often asserted that the Indian banking sector is saddled with too many branches, adding to its high intermediation costs. In fact, at about 8-10,000, the population per branch in developed countries is lower than that in India. Therefore, the reform process has maintained the gains in terms of the outreach of bank branches achieved in the phase of social banking. Despite a decline, direct lending to disadvantaged segments of the economy under the priority sector advances remained high during the reform period. The decline in priority sector lending since the initiation of reforms in fact reflects greater flexibility provided to banks to meet such targets. Currently, in the event a bank fails to meet the priority sector lending target through direct lending, the bank can invest the shortfall amount with the apex organizations dealing with flow of funds towards agriculture and small-scale industries. While adherence of banks to the norms on direct lending towards the priority sector still remains desirable, the current arrangement reflects how the reform process has provided operational flexibility to banks even while meeting social objectives.

FUTURE CHALLENGES FOR INDIAN BANKS

A few broad challenges facing the Indian banks are: threats of risks from globalisation; implementation of Basel II; improvement of risk management systems; implementation of new accounting standards; enhancement of transparency and disclosures; enhancement of customer service; and application of technology. *Globalisation – a challenge as well as an opportunity* The waves of globalisation are sweeping across the world, and have thrown up several opportunities accompanied by concomitant risks. Integration of domestic market with international financial markets has been facilitated by tremendous advancement in information and communications technology. There is a growing realisation that the ability of countries to conduct business across national borders and the ability to cope with the possible downside risks would depend, *inter alia*, on the soundness of the financial system. This has necessitated convergence of prudential norms with international best practices as well consistent refinement of the technological and institutional framework in the financial sector through a non-disruptive and consultative process.

OPENING UP OF THE CAPITAL ACCOUNT

The Committee on Fuller Capital Account Convertibility (Chairman: Shri S.S. Tarapore) observed that under a full capital account convertibility regime, the banking system would be exposed to greater market volatility, and this necessitated enhancing the risk management capabilities in the banking system in view of liquidity risk, interest rate risk, currency risk, counter-party risk and country risk that arise from international capital flows. The potential dangers associated with the proliferation of derivative instruments – credit derivatives and interest rate derivatives also need to be recognised in the regulatory and supervisory system. The issues relating to cross-border supervision of financial intermediaries in the context of greater capital flows are just emerging and need to be addressed.

BASEL II IMPLEMENTATION

The Reserve Bank and the commercial banks have been preparing to implement Basel II, and it has been decided to allow banks some more time in adhering to new norms. As against the deadline of March 31, 2007 for compliance with Basel II, it was decided in

October 2006 that foreign banks operating in India and Indian banks having presence outside India would migrate to the standardised approach for credit risk and the basic indicator approach for operational risk under Basel II with effect from March 31, 2008, while all other scheduled commercial banks are required to migrate to Basel II by March 31, 2009. It is widely acknowledged that implementation of Basel II poses significant challenge to both banks and the regulators. Basel II implementation may also be seen as a compliance challenge. But at the same time, it offers two major opportunities to banks, *viz*., refinement of risk management systems; and improvement in capital efficiency. The transition from Basel I to Basel II essentially involves a move from capital adequacy to capital efficiency. This transition in how capital is used and how much capital is needed will become a significant factor in return-onequity strategy for years to come. The reliance on the market to assess the riskiness of banks would lead to increased focus on transparency and market disclosure, critical information describing the risk profile, capital structure and capital adequacy. Besides making banks more accountable and responsive to better-informed investors, these processes enable banks to strike the right balance between risks and rewards and to improve the access to markets. Improvements in market discipline also call for greater coordination between banks and regulators.

IMPROVING RISK MANAGEMENT SYSTEMS

Basel II has brought into focus the need for a more comprehensive risk management framework to deal with various risks, including credit and market risk and their inter-linkages. Banks in India are also moving from the individual silo system to an enterprise-wide risk management system. While the first milestone would be risk integration across the entity, the next step would entail risk aggregation across the group both in the specific risk areas as also across the risks. Banks would, therefore, be required to allocate significant resources towards this endeavour. In India, the risk-based approach to supervision is also serving as a catalyst to banks' migration to the integrated risk management systems. However, taking into account the diversity in the Indian banking system, stabilizing the RBS as an effective supervisory mechanism is another challenge.

CORPORATE GOVERNANCE

To a large extent, many risk management failures reflect a breakdown in corporate governance which arise due to poor management of conflict of interest, inadequate understanding of key banking risks, and poor Board oversight of the mechanisms for risk management and internal audit. Corporate governance is, therefore, the foundation for effective risk managements in banks and, thus, the foundation for a sound financial system. Therefore, the choices which banks make when they establish their risk management and corporate governance systems have important ramifications for financial stability. Banks may have to cultivate a good governance culture building in appropriate checks and balances in their operations. There are four important forms of oversight that should be included in the organisational structure of any bank in order to ensure appropriate checks and balances: (i) oversight by the board of directors or supervisory board; (ii) oversight by individuals not involved in the day-to-day running of the various business areas; (iii) direct line supervision of different business areas; and (iv) independent risk management, compliance and audit functions. In addition, it is important that key personnel are fit and proper for their jobs. Furthermore, the general principles of sound corporate governance should also be applied to all banks, irrespective of their unique ownership structures.

IMPLEMENTATION OF NEW ACCOUNTING STANDARDS

Derivative activity in banks has been increasing at a brisk pace. While the risk management framework for derivative trading, which is a relatively new area for Indian banks (particularly in the more structured products) is an essential pre-requisite, the absence of clear accounting guidelines in this area is a matter of significant concern. The World Bank's ROSC on Accounting and Auditing in India has commented on the absence of an accounting standard which deals with recognition, measurement and disclosures pertaining to financial instruments. The Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI) is considering issue of Accounting Standards in respect of financial instruments. These will be the Indian parallel to International Accounting Standards 32 and 39. The proposed Accounting Standards will be of considerable significance for financial entities and could, therefore, have implications for the financial sector. The formal introduction of these Accounting Standards by the ICAI is likely to take some time in view of the processes involved. In the meanwhile, the Reserve Bank is considering the need for banks and financial entities adopting the broad underlying principles of IAS 39. Since this is likely to give rise to some regulatory/prudential issues, all relevant aspects are being comprehensively examined. The proposals in this regard would, as is normal, be discussed with the market participants before introduction. Adoption and implementation of these principles are likely to pose a great challenge to both the banks and the Reserve Bank.

SUPERVISION OF FINANCIAL CONGLOMERATES

The financial landscape is increasingly witnessing entry of some of the bigger banks into other financial segments like merchant banking, insurance etc. Emergence of several new players with diversified presence across major segments makes it imperative for supervision to be spread across various segments of the financial sector. In this direction, an inter-regulatory Working Group was constituted with members from RBI, SEBI and IRDA. The framework proposed by the Group is complementary to the existing regulatory structure wherein the individual entities are regulated by the respective regulators and the identified financial conglomerates are subjected to focused regulatory oversight through a mechanism of inter regulatory exchange of information. As a first step in this direction, an inter-agency Working Group on Financial Conglomerates (FC) comprising the above three supervisory bodies identified 23 FCs and a pilot process for obtaining information from these conglomerates has been initiated. The complexities involved in the supervision of financial conglomerates are a challenge not only to the Reserve Bank of India but also to the other regulatory agencies, which need to have a close and continued coordination on an on-going basis. In view of increased focus on empowering supervisors to undertake consolidated supervision of bank groups and since the Core Principles for Effective Banking Supervision issued by the Basel Committee on Banking Supervision have underscored consolidated supervision as an independent principle, the Reserve Bank had introduced, as an initial step, consolidated accounting and other quantitative methods to facilitate consolidated supervision. The components of consolidated supervision include, consolidated financial statements intended for public disclosure, consolidated prudential reports intended for supervisory assessment of risks and application of certain prudential regulations on group basis. In due course, consolidated supervision as introduced above would evolve to cover banks in mixed conglomerates, where the parent may be non-financial entities or parents may be financial entities coming under the jurisdiction of other regulators.

APPLICATION OF ADVANCED TECHNOLOGY

The role of technology in banking in creating new business models and processes, in maintaining competitive advantage, in enhancing quality of risk management systems in banks, and in revolutionising distribution channels, cannot be over emphasised. Recognising the benefits of modernising their technology infrastructure, banks are taking the right initiatives. While doing so, banks have four options to choose from: they can build a new system themselves, or buy best of the modules, or buy a comprehensive solution, or outsource. A further challenge which banks face in this regard is to ensure that they derive maximum advantage from their investments in technology and avoid wasteful expenditure which might arise on account of uncoordinated and piecemeal adoption of technology; adoption of inappropriate/ inconsistent technology and adoption of obsolete technology. A case in point is the implementation of core banking solution by some banks without assessing its scalability or adaptability to meet Basel II requirements.

FINANCIAL INCLUSION

While banks are focusing on the methodologies of meeting the increasing demands placed on them, there are legitimate concerns with regard to the banking practices that tend to exclude rather than attract vast sections of population, in particular pensioners, self-employed and those employed in unorganised sector. While commercial considerations are no doubt important, banks have been bestowed with several privileges, especially of seeking public deposits on a highly leveraged basis, and consequently they should be obliged to provide banking services to all segments of the population, on equitable basis. Further, experience has shown that consumers' interests are at times not accorded full protection and their grievances are not properly attended to. Feedback received reveals recent trends of levying unreasonably high service/user charges and enhancement of user charges without proper and prior intimation. It is in this context that the Governor, Reserve Bank of India had mentioned in the Annual Policy Statement 2005-06 that RBI will take initiatives to encourage greater degree of financial inclusion in the country; setting up of a mechanism for ensuring fair treatment of consumers; and effective redressed of customer grievances.

CONCLUSION

With the increasing levels of globalisation of the Indian banking industry, evolution of universal banks and bundling of financial services, competition in the banking industry will intensify further. The banking industry has the potential and the ability to rise to the occasion as demonstrated by the rapid pace of automation which has already had a profound impact on raising the standard of banking services. The financial strength of individual banks, which are major participants in the financial system, is the first line of defence against financial risks. Strong capital positions and balance sheets place banks in a better position to deal with and absorb the economic shocks.

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