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RESERVE BANK OF INDIA

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RBI releases June 2014 Financial Stability Report

The Reserve Bank of India today released the Financial Stability Report (FSR) June 2014, the ninth issue of the half-yearly publication.

The FSR reflects the collective assessment of the Sub-Committee of the Financial Stability and Development Council (FSDC), on risks to financial stability. The Report aims to promote awareness about the vulnerabilities in the financial system, to inform about the resilience of the financial institutions and to encourage debate on issues relating to development and regulation of the financial sector.

The latest issue is being brought out at a time when global financial markets are showing signs of improved stability although growth is still not on strong ground and easy monetary policy continues in many jurisdictions. On the domestic front, the return to political stability has provided impetus to the outlook and the capital markets reflect the expectations on policy measures to address the adverse growth-inflation dynamics and saving-investment balance as also efficient implementation of policies and programmes.

India's financial system remains stable, though the banking sector is facing some major challenges, mainly relating to public sector banks (PSBs). Although there has been some improvement in the asset quality of scheduled commercial banks (SCBs) since September 2013, the level of gross non-performing advances as percentage of total gross advances (GNPA ratio) of PSBs was significantly higher as compared to the other bank groups. While the ownership pattern and recapitalisation of PSBs are contingent upon government policy and the fiscal situation, there is a case for reviewing the governance structures of PSBs, with a greater emphasis on market discipline.

Macro stress tests show that the system level capital to risk-weighted assets ratio (CRAR) of SCBs remains well above the regulatory minimum even under adverse macroeconomic conditions.

The regulation of securities markets in India is in sync with international developments, although mutual funds and other asset management activities in Indian markets do not carry risks similar to those experienced in other jurisdictions. The lending activity of insurance companies, though relatively small and within the prescribed exposure limits applicable for insurance companies, may need to be streamlined and monitored under a prudential framework comparable to that for banks to eliminate the possibility of regulatory arbitrage. Revised norms for corporate governance as also warehouse and related processes are expected to strengthen the functioning of the commodity derivatives market. In the context of India's pension sector, inadequate liability computation in case of several defined benefit pension schemes can be a potential source of fiscal stress in years to come.

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