IIMB Management Review (2016) 28, 170–178

available at www.sciencedirect.com
ScienceDirect
journal homepage: www.elsevier.com/locate/iimb

ROUND TABLE

India emerging: New financial architecture

Sankarshan Basu *

Finance & Accounting, Indian Institute of Management Bangalore, Bangalore, Karnataka, India

Received 28 June 2016; accepted 27 July 2016; available online 15 August 2016

KEYWORDS
New financial architecture;
Integrated financial architecture;
De-regulation;
Global Financial Crisis 2007–2008;
Banking;
Mutual funds;
Non-banking finance companies;
Risk management

Abstract The global financial crisis of 2007–2008 highlighted the need to re-evaluate several well established tenets in the world of finance. Questions have been raised the world over about the existing paradigm, leading to an acceptance that new financial architecture needed to be evolved and that new models need to emerge, keeping in mind the multiplicity of socio-economic realities that exist round the globe. In this context, the imperative for a new financial architecture in India is quite evident, and the ensuing panel discussion throws up some India-specific issues that need to be explored by the various stakeholders involved in this attempt.
© 2016 Production and hosting by Elsevier Ltd on behalf of Indian Institute of Management Bangalore. This is an open access article under the CC BY-NC-ND license (http://creativecommons.org/licenses/by-nc-nd/4.0/).

Perspective note to round table

The global financial crisis of 2007–2008 has questioned many of the beliefs held very strongly in the world of finance, in particular about the way the whole system was developed and sustained. The collapse of most of the large financial institutions in the capitalist capital of the world, the United States of America, and the subsequent requirement of huge governmental support in bailing out these institutions to preserve the stability of the social structure have led to regulators (both national and international), policy makers, researchers as well as practitioners questioning the very model on which they had built their reputation, leading to an understanding of the requirement for a new financial architecture to be followed, going forward.

We are now at the point where the need for the new financial architecture has been more or less universally accepted, but the exact form of the same is yet to be understood and accepted. In fact, it is highly probable that there will be not just one model but multiple models depending on the underlying social fabric and requirements, and hopefully all of the models will coexist.

The financial architecture that has been in use was conceived in the wake of the Great Depression of 1929 and was designed to address the issues arising out the economic conditions at that point. Over the last 70 odd years, the economic conditions around the globe have significantly changed. The Second World War and the development assistance plans that were put in place post the war by the developed nations meant that there was an abundance of capital to rebuild the

* Fax: +91 80 2658 4050.
E-mail address: sankarshanb@iimb.ernet.in.

http://dx.doi.org/10.1016/j.iimb.2016.07.004
0970-3896 © 2016 Production and hosting by Elsevier Ltd on behalf of Indian Institute of Management Bangalore. This is an open access article under the CC BY-NC-ND license (http://creativecommons.org/licenses/by-nc-nd/4.0/).

world. This also meant that a lot of the regulators' frameworks put in place in the immediate aftermath of the Great Depression were slowly but steadily dismantled; so much so that by the 1990s the entire financial markets globally (particularly the developed world) were subject to very little regulation.

On the other hand, financial markets in countries like India and China were still significantly controlled by the regulators, and in some cases by the governments themselves. In the good years, through until about 2006–2007, this meant that the perceived benefit of deregulation that most of the developed markets saw did not really percolate to these markets and hence these markets had a persistent demand for larger levels of deregulation. This has been coupled with the need for relatively high growth rates that these countries would require to sustain their economies—a growth rate of 8%–9% going forward for a number of years. One of the obvious fallouts of these kinds of needs would be the fact that the standard financial architecture that existed would not be able to sustain this level of growth—in fact no one segment of the financial sector will be able to sustain the growth required; hence the possible need for an integrated new financial order or architecture integrating the banking sector, the mutual funds, and the non-banking finance sector. Another sector that probably would need to be formally included in this new order would be the organisations that collate and provide all the relevant financial information—as, going forward, information will be the key driver and more so in the financial sector.

While the new financial architecture needs to be developed, each segment of the finance industry will be impacted. The banking segment will probably the most impacted as it is the largest contributor to the financial sector. The need for financial inclusion in the country, the push for the same from the government, as well as the additional responsibilities and requirements thrust on them on account of the various regulatory mechanisms, for example the Basel guidelines, will definitely make banking a whole new ball game when compared to the banking sector that we now know of. Implementation of and adherence to such requirements would also require significant amount of trained human capital and thus trained human capital would also form a pillar in the new financial architecture that is in the process of being developed.

The other major sector that probably has never got the attention due to it is the micro small and medium enterprises (MSME). It seems clear that these MSMEs are going to be the major drivers of growth in the future and hence the entire financial structure would have to give importance and prominence to the capital and fund requirements for such enterprises; this is particularly relevant given that the current share of the non-corporates in the Indian GDP is about 52% and is expected to grow in the coming years. The financial support needs to come from the formal banking sector as well as the non-formal sector represented by the non-banking financial companies (NBFCs). Interestingly NBFCs can also play a significant part in the financial inclusion of all citizens. In a sense, it is now clear that going forward, NBFCs will play an even larger role than it plays currently and such organisations will have to be given a place at the high table of finance on equal terms.

The other pillar of the new financial architecture will be the mutual fund industry. Globally it is already a very important player contributing around 36% of the global GDP. This number is only expected to increase with increased life expectancy and therefore an increase in the superannuated population leading to larger savings during the working life. On the contrary mutual funds contribute only about 7% to the Indian GDP; but as life expectancy increases, the retired population also increases, and thus the need for increased savings will become very important, and the mutual funds will be one of the prime vehicles of this investment going forward. The main driver that will lead to a successful increase in the increased investments in mutual funds will be improved and effective regulation of the capital markets, thereby increasing the confidence of the common investor in capital market products and, as a consequence, the mutual funds.

The final pillar of this new financial architecture has to be information—information on all counts but in particular channelised towards risk management and risk mitigation. The same is being highlighted by all regulators—Basel guidelines by the Bank of International Settlements (BIS) is a classic case in point. The importance is also growing as better and more efficient analytics tools are available today for users and regulators alike to carry out detailed predictive analysis and hence try and pre-empt adverse market moves. Even if the success of pre-emptive market moves may be questioned, the ability of these data based strategies will give all the stakeholders of the financial system a better chance to have more efficient and robust risk management systems—not that they will be successful all the time but the success rate will definitely improve significantly from the current times and thus improve the efficiency of the entire financial sector.

In this context, the imperative for a new financial architecture in India is evident. The following panel discussion brings forth some of the issues that would need to be identified, particularly in the Indian case, as the regulators and the policy makers in conjunction with market participants go about building a new architecture.

India emerging: New financial architecture—panel discussion[1]

Chair: R. Vaidyanathan

Professor, Finance & Control, Indian Institute of Management Bangalore

Panellists:

T. Keshav Kumar, Chief General Manager, Commercial Banking, State Bank of Mysore

Imtaiyazur Rahman, Chief Financial Officer, UTI Mutual Fund

Sriram Ramnarayan, Country Head, Financial Markets, Thomson Reuters

G. S. Sundararajan, Group Director, Shriram Group.

[1] The panel discussion was part of the 4th India Finance Conference 2014, December 17–19, 2014. This part of the article carries edited excerpts of the presentations made at the panel discussion. The views expressed by the panellists are personal and academic in nature and not necessarily the views of their organisations. The presentations of the panellists were made in an academic context in an academic institution. The data and statistics are as quoted by the panellists in their presentations.

Download English Version:

https://daneshyari.com/en/article/5109249

Download Persian Version:

https://daneshyari.com/article/5109249

Daneshyari.com