

How much emphasis banks give to best practices and business processes in order to handle the changed financial scenario today? Executive directors of four leading banks speak to executive editor N. Mohan on their perspectives:

Countering the Melttdown



A report in early 2008 by consultants McKinsey & Co revealed that while India's banks fared well by global standards on several counts, including shareholder value, they need to do much more in order to stay competitive in a scenario where they have to service customers with global options. The study undertaken by the consultants for the Indian Banks Association covered 14 Indian banks - seven public sector banks, four private sector banks and three foreign banks - and judged them in terms of personal financial services, retail banking, IT benchmarks, organizational performance and asset liability management. Indian banks have unprecedented opportunities, the report said, and added that it is now time for them to look at how well they are positioned for continued growth. The banks performed remarkably in two aspects, McKinsey said, - in increasing shareholder value and in allocating capital efficiently. They also did well in contributing to India's GDP on a global scale. However, they lagged behind in several aspects. One another factor brought out in the report pertains to credit and risk best practices. On this measure, 'Indian banks fare well against their global peers,' says the report, elaborating that this measure covered banks' performance on credit underwriting, rating, risk-based pricing, credit portfolio management and credit monitoring. On a scale of 0 to 4, the consulting firm gives Indian private banks the top score of 3.3, while the top global banks average 3.2 and Asian banks average 3.1.

So, in a scenario of global meltdown and the resultant tightening of the financial governance, have the banks felt it necessary to bring about changes in their best practices? How do they evolve processes? Do they prescribe quality standards? And to what extent external consultants are involved in creating the processes? Banking Frontiers covered four major banks in the country - two public sector and two private sector - to get a representative view.

All the banks felt that best practices are inherent in the

operations and these are in constant transformation to suit any changing environment. Processes and systems too are very much in place and suitably modified and enhanced in order to meet any unpredictable eventualities.

ONGOING TRANSFORMATION PROCESS

"Switching over to the best banking practices is an ongoing transformation process to bring about newer changes in processes and dispensation of financial services," says V. Santhanaraman, executive director, Bank of Baroda. Tracing how the financial sector reforms in the country had led to banks adopting international best practices to combat the rising competitive environment and tough market conditions, Santhanaraman says "From the macro strategic planning process to the grass root level of service dispensation, the quality with due diligence took the utmost attention of the banking sector."

In the past, Bank of Baroda had undertaken several business initiatives to bring about changes in business approach and processes to become the source that would help its stakeholders realize their goals. "As part of all these ongoing efforts, the bank has adopted a slew of best practices in risk management, capital management, customer services, IT operations and credit and treasury products," says Santhanaraman.

He is of the view that best practices in banks need to be adopted on a daily basis. The bank has to some extent been traditional in its approach - especially in giving liberties to its staff and in delegating powers - and this has helped the bank in containing risks. The bank has a legacy of more than 100 years and the processes and systems that are in place in the bank have withstood the test of time.

"Having said this, I would wish to emphasize that once you offer quality products and services and exert controls at the required levels, everything else will follow. Some of our innovative services like the 8 a.m. to 8 p.m. banking, which is available at some

500 branches, 24-hour banking at select branches are steps in this direction. We understand the specific requirements of the customers and devise processes to facilitate servicing them in a better and efficient manner. In order to do this, we segment the customers as per their requirements and meet their specific needs. The Retail and SME Loan Factories are some of the examples where we have geared our services and products to the exact requirements of the target audience. Similarly, we have several HR initiatives in the bank, which have helped mould leaders and optimally use manpower resources. The effort has been to build up a team that is geared to meet the changing requirements in the banking sector," says he.

V.K. Ramani, executive director (Technology and Business Processes), Axis Bank, says in the banking industry best practices are always there whether it is in good times or bad times. "What happens is that lending norms depend on the market situations and requirements. The processes and systems that govern business best practices largely depend on the risk perceptions - credit risk, interest rate risk and operations risk. In today's banking operations, there is a highly relevant need for robust risk management programs."

BASEL II NORMS

Ramani emphasizes that the best practices requirements for banks are inherent in the Basel II regulations. Indian banks have now to adhere to Basel II norms and have to mandatorily follow the norms and processes prescribed. "Risk management and risk mitigation are therefore part of the program and banks need not worry about these. However, there could be situational changes on a short term basis and banks will be able to carry through with some strategic adjustments and modified priorities. At Axis Bank what we do have is a full-fledged and highly focused risk management department, which is always conversant with the market situations. The members look at sectoral exposure and industry exposure and they also look out for any rating downgrade of companies we had lent. They are specialists in their own right to address risk management issues."

S.C. Kalia, executive director, Vijaya Bank, too says sometimes external triggers prompt further fine tuning of business practices. "For Vijaya Bank, being a 78-year old public sector bank, our business practices have been time tested and are reasonably in sync with demands of a fast changing operating environment. I must also say that, unlike the corporate world, a public sector bank's business processes are considerably influenced by the regulatory and supervisory practices as well. Take for instance, the issue of possible overheating in the realty market about a year back. A spate of regulatory moves to preempt possible bubbles was duly factored into the banks' business strategies. Besides, there have been stipulations regarding exposure to sensitive sectors



V. Santhanaraman



S. C. Kalia

which form part of the banks' business practices. Thanks to the regulatory safeguards and banks' proactive stance, India did not have a free fall in its asset market as seen recently in the West."

Kalia says in Vijaya Bank, apart from taking due cognizance of regulatory norms, considerable changes in the internal systems and procedures have been made. "For instance, we rely as much on cash flow aspects as on collaterals while appraising loan proposals. Problems of mortgage markets in

the US and elsewhere have clearly taught us that collateral may be a necessary but not a sufficient condition in loan proposals. Effectiveness in review and monitoring mechanism is another dimension of business process reengineering. Thanks to CBS, we have adopted a graded approach to assessing the quality of our loan books. Through a designated 'special watch' category, we keep monitoring and safeguarding those assets which show signs of slippage. Apart from text book basics, we also rely on 'learning by doing' on a day-to-day basis. We have recently introduced Online Processing of Loan Applications for client convenience which we are subjecting to repeated trials and counterchecks before it stabilizes."

K.S. Harshan, executive director, Federal Bank, has a different view. Says he: "Best practices governing business, to me, are not alterable based on the economic environment. We cannot have one set of best practices for good times one for not so good times. Then they become 'best practices of convenience' and will not be acceptable. Therefore, I do not think it would be proper to touch best practices unless they are outdated and deeply away from the broad contemporary governance standards of business. Changing best practices to suit economic environment is therefore is out of question."

As far as the current scenario is concerned, Harshan says there are no 'tightening of lending norms' by banks. What is happening is that the banks are re-looking at certain sectoral exposures, which are more vulnerable during the down turn.

EFFECTIVE LIQUIDITY MANAGEMENT

Santhanaraman points out that the recent liquidity crises brought forth the fact that liquidity management is the most crucial aspect of any bank's survival. He also adds that most of the risks are directly connected with liquidity. And at Bank of Baroda, the risk management processes are very rugged and efficient. In fact, the bank has been one of the first to adopt BASEL II. It is a question of how effectively the bank has been able to manage liquidity and how robust its asset quality is. "We had no problem with liquidity at any period of time. We have a substantial international presence and mind you at no point of time we had to provide funds support from India for the international operation. The bank has an excellent credit monitoring system. It has an integrated treasury operation covering forex, money

management, equity operations, and bond operations," he says.

Santhanaraman says banks should be worried about credit risk, market risk and operational risk. To this extent, the risk management and mitigation processes in Bank of Baroda are very much in place. The bank has implemented standardized approach for credit risk and standardized duration approach for market risk and basic indicator approach for operational risk in line with the RBI's guidelines. "And I am confident to say through the adoption of BASEL II norms, the bank has been able to create systems and norms for managing all these risks. Risk management and mitigation processes are parameterized and review of these parameters is a continuous process for us. Besides, there are technology interventions at appropriate levels which make the risk management more efficient and error-proof."

Ramani of Axis Bank agrees that liquidity is an important aspect in banking operations. A better liquidity is maintained through effective asset liability management. This is managed by the Asset Liability Committee, or ALCO, which looks at factors including maturity pattern of deposits and managing funding needs for various sectors. The disbursement patterns are monitored, the maturity period of the deposits are monitored. The monitoring process, however, largely depends on market conditions, largely driven by the behavior of the market. The short term interest rates may go up or come down. So liquidity monitoring is carried out on a week-to-week basis.

Says he: "At Axis Bank, we already have processes in place, which are geared to generate quick response to any given situation. This is largely achieved through a structured information management system. As part of our risk management team, there is an economic research department, which carries out macro analysis, tracks down changes in monetary policies and studies how the economy of the country is faring. The economists in this department are specially recruited for this purpose. The inputs strengthen our risk management processes."

PROCESS RE-ENGINEERING

How do banks give effect to changes in processes? Is it based on internal discussions or are there external consultants involved?

Kalia of Vijaya Bank says most of the process-related changes have emanated from within the organization and through various forums / committees. The bank has a dedicated systems and procedures committee headed by the executive director and its meetings involve lot of brain churning on possible changes, based on feedback from other players and the bank's own employees. It also has steering committees on technology which delves in-depth and decides on changes in business processes on a regular basis.



K.S. Harshan



V.K. Ramani

Santhanaraman categorizes the bank's activities into strategic business initiatives, leadership development and business process re-engineering and organizational restructuring. In strategic business initiatives, the bank had undertaken a growth strategy and business transformation initiative to evolve business strategies and business models in 2006, called 'Project Parivartan'. The bank engaged an outside consultant, McKinsey and Co, for this purpose. The aim was to evolve a five-year

strategy plan for achieving business growth, to identify revenue streams, new profit centers and new customer segments. The retail loan factories of the bank are a result of this exercise. The retail loan factories work on assembly line principle aimed to reduce turnaround time and enable and ensure timely disbursement of retail loans at branches. In leadership development, the bank is readying its staff to face the challenges of 21st century and the competition in the banking realm. The bank engaged a consultant, Right Management, to advise it on developing and executing a customized leadership development program. The bank has also taken steps to evolve a business process re-engineering and organizational restructuring initiative to realize its vision 2010.

For Ramani business process re-engineering is a continuous process. "There is one or other change happening every year during the last eight years. We are not in a static state at any time."

Harshan of Federal Bank is of the view that credit delivery processes are not dependent on the economic conditions. These processes are evolved over the years based on changing customer expectations, technology, cost and operational risk. "Given the current scenario, what is relevant is to have a re-look at the underwriting (sanctioning norms). I am sure that every bank is on that process now. Such reviews, typically, will focus on certain benchmark norms such as DER and the gearing ratios, which we also lay emphasis upon like any lenders," says he.

How would they describe the respective bank's approach in creating processes - innovative, reactive or proactive?

Santhanaraman says it has to be a combination. "At Bank of Baroda, we have been innovative and the examples are our retail and SME loan factories, the change in our logo, which could visibly create awareness about the bank and which was successfully followed by other public sector banks. To a large extent, we have been proactive and the systems and processes in place have been quite instrumental in preventing untoward incidents. To some extent, we have to be reactive as we cannot prophecy all that are bound to happen."

At Axis Bank, says Ramani, processes and systems are evolved, which are a mix based on facts and analyses.

Harshan is more forthcoming. He says he would describe it as proactively innovative. "Each product we sell and service we

offer has its own processes at the front-end (customer facing) and backend (non-customer facing). Competition and rising customer expectations have in fact are forcing banks to revisit all the existing processes to bring down the turn around time and reduce cost without sacrificing on security and risk," he says.

While the bank reviews existing product processes periodically, processes associated with new products are designed with these aspects in mind. With the prevalence of high level of technology in the bank, it has been able to constantly innovate and address issues proactively. "The fact that the issue of process reengineering was an important focus area while migrating to CBS demonstrates our philosophy," he adds.

TECHNOLOGY IS PRIME

That brings to fore the role of technology and how it has facilitated the process changes.

According to Kalia of Vijaya Bank, technology did have a catalytic and enabling role in smoothening the changes in business processes. "We have 97% of our business covered under CBS and we aim to make it 100% by March 2009. We have been leveraging CBS to good effect in many spheres, be it in matters like launching and convergence of delivery channels or back office processing. For example, we have recently introduced V-Payroll deposit scheme targeted at the salaried class. The response has been quite overwhelming and in order to deal with huge processing jobs, we have set up BPO units at select regions. This has enabled branches to focus more on business development."

Harshan says technology has played an important role in innovating processes. Besides reducing cost and the overall turnaround time in respect of several products, it has also helped the bank to standardize. "Going forward processes will become more technology and system dependent," he adds.

In Axis Bank, technology plays an integral part in its business strategy. Process changes that can significantly reduce operational costs are put in place from time to time. Ramani says technology is all-pervasive in the bank. "It is entrenched in the way the bank functions. Technology's is not just a role. It is an inherent part of all our operations and businesses. It has been a major resource in our business activities."

Bank of Baroda, feels Santhanaraman, has been a late entrant as far as adoption of technology is concerned. This has in fact helped the bank to some extent, because it could skip the trial and error period. "We got to implement the core banking solution in 2005 when the software was comparatively mature and several extensions have come in place. Our implementation too has been quite fast in that by 2008 we could bring about 92% of our branches under CBS. In addition, we have been able to offer our customers e-banking, mobile and internet banking and other facilities. Our cash management system is quite robust. Technology has also enabled us to have our own data warehousing and backoffice facilities."

The bank is now into document imaging and once this technology is perfected, it expects a lot of efficiency added to the services and products. Santhanaraman says: "We are

also planning to set up online surveillance system and online monitoring system whereby branches can be inspected remotely. We will be able to see actual operations happening in remote places sitting at the corporate office. This will help us cut down on manpower and effect time and cost savings and at the same time take timely and appropriate decisions."

Bank of Baroda had engaged consultants Gartner to suggest strategic business model based on the best global practices for leveraging technology for business development. Gartner had suggested a business transformation plan based on various lines of business and the principle of customer segmentation. It has also proposed to upgrade the existing IT setup in the bank to make it more conducive in implementing the business transformation plan. "Keeping in line with the global best practices, we have embraced and pursued on the business transformation plan with process reengineering and technology enablement. Later Hewlett Packard was appointed as the system integrator to provide an end-to-end technological solution in the ambit of the business transformation plan," adds Santhanaraman.

QUALITY STANDARDS

What about benchmarks for quality and adoption of standards like ISO certifications, Six Sigma or Lean?

"No, we have not opted for these branded quality standards," says Santhanaraman. "However, our processes and systems are quite akin to these standards. What is ultimate in our minds is customer satisfaction and we reset our processes and systems to achieve this. Our strategy has been to go to the source of the customer complaint - what actually causes the complaint - and rectify it at the root level rather than address the complaint at the peripheral level. Changes are then done at the systems level and in some cases even carry out the changes with retrospective effect. We have quite perfected this strategy. Technology has helped us in this effort," he says.

Harshan too says Federal Bank's processes are originally designed with the customer in mind, simultaneously addressing the risk associated. "These processes have in fact stood the test of time. It was perhaps one of the reasons behind our success and growth over the last several decades. However we are conscious of the emerging standards and as we grow in size and network we believe we may have to go in for certain certifications like other players."

In Axis Bank, the audit process is ISO-certified. Ramani says the bank's information security processes function on the basis of international benchmarks.

While Bank of Baroda has engaged consultants (McKinsey and Co, Right Management and Gartner) in order to define and advise it on various processes, Federal Bank has so far not engaged any external consultants to advise it on processes. Ramani of Axis Bank says the bank takes consultants for specific tasks depending on given situation and business needs. "We identify a problem and if this cannot be tackled through our internal resources, we engage a consultant to advise us on this specific problem. There are no omnibus consultants, who will always be there at the bank."

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