CHAPTER- 2

REVIEW OF LITERATURE
2.1 INTRODUCTION

The understanding of any subject depends on a good knowledge of related literature. A good knowledge of the related literature helps not only to find out the scope of the subject but also to design the study in an improved manner. A brief review of the available studies in this field and related fields is attempted in the following paragraphs.

Every one of us knows that human life and possession of assets are frequently exposed to loss or damage because of various reasons. There is a great deal of uncertainty and risk in life as well as in industry. Since people are aware of this uncertainty and risk of their lives and possessions they show a strong desire for security. The need for security is sought by taking all precautions possible to avoid or prevent the consequences of risk. Risk Management and Risk based Supervision in Banks has been the subject of study of many Agencies and Researchers and Academicians. There is a treasure of literature available on the subject.

A careful selection of relevant material was a difficult task before the Researcher. Efforts have been made to scan the literature highly relevant to the Context. The main sources of literature have been the Website of the Reserve Bank of India, the website of the Basle Committee on Banking Supervision and the websites of several major Banks both in India and abroad. The publications of Academicians engaged in the Risk Management and Central Banking Supervision sphere also throws valuable insights into the area. The occasional Research papers published by Reserve Bank, the speeches of the Governor and the Deputy Governors of the Reserve Bank of India, the Publications of the Reserve Bank of India, the Indian Banks Association have proved quite relevant to the study.
2.2 LITERATURE REVIEW - INTERNATIONAL PERSPECTIVE

Crouhy, Gala, Marick (2006) have summarised the core principles of Enterprise wide Risk Management. As per the authors Risk Management culture should percolate from the Board Level to the lowest level employee. Firms will be required to make significant investment necessary to comply with the latest best practices in the new generation of Risk Regulation and Management. Corporate Governance regulation with the advent of Sarbanes-Oxley Act in US and several other legislations in various countries also provide the framework for sound Risk Management structures. Hitherto, Enterprise wide Risk Management existed only for name sake. Generally firms did not institute a truly integrated set of Risk measures, methodologies or Risk Management Architecture. The ensuing decades will usher in a new set of Risk Management tools encompassing all the activities of a Corporation. The integrated Risk Management infrastructure would cover areas like Corporate Compliance, Corporate Governance, and Capital Management etc. Areas like business risk, reputation risk and strategic risk also will be incorporated in the overall Risk Architecture more formally. As always it will be the Banks and the Financial Services firms which will lead the way in this evolutionary process. The compliance requirements of Basel II and III accords will also oblige Banks and Financial institutions to put in place robust Risk Management methodologies.

The authors felt that it is generally felt that Risk Management concerns largely with activities within the firm. However, during the next decade Governments in different countries would desire to have innovatively drawn Risk Management system for the whole country. The authors draw reference to the suggestions of Nobel Laureate Robert Merton who suggested that a country with exposure to a few concentrated industries should be obliged to diversify its excessive exposures by arranging appropriate swaps with other countries with similar problems. Risk
Management offers many other potential macro applications to improve the management of their social security measures etc. They draw references to the spread of Risk Management Education worldwide.

**Carl Felsenfeld (2007)** outlined the patterns of international Banking regulation and the sources of governing law. He reviewed the present practices and evolving changes in the field of control systems and regulatory environment. The book dealt a wide area of regulatory aspects of Banking in the United States, regulation of international Banking, international Bank services and international monetary exchange. The work attempted in depth analysis of all aspects of Bank Regulation and Supervision.

Money Laundering has been of serious concern worldwide. Its risk has wide ramifications. Money Laundering has lead to the fall of Banks like BCCI in the past. In this context the book on Anti-Money Laundering: International Practice and Policies by John Broome Published by Sweet and Maxwell (August 2005) reviews the developments in the area of Money Laundering. The author explains with reference to case studies the possible effects of Money Laundering. The book gives a comprehensive account of the existing rules and practices and suggests several improvements to make the control systems and oversight more failsafe.

**Hannan and Hanweck (1988)** felt that the insolvency for Banks become true when current losses exhaust capital completely. It also occurs when the return on assets (ROA) is less than the negative capital-asset ratio. The probability of insolvency is explained in terms of an equation. The help of Z-statistics is commonly employed by Academicians in computing probabilities.
Daniele Nouy (2008) elaborates the Basel Core Principles for effective Banking Supervision, its innovativeness, content and the challenges of quality implementation. Core Principles are a set of supervisory guidelines aimed at providing a general framework for effective Banking supervision in all countries. They are innovative in the way that they were developed by a mixed drafting group and they were comprehensive in coverage, providing a checklist of the principal features of a well designed supervisory system.

The core Principles specify preconditions for effective banking supervision characteristics of an effective supervisory body, need for credit risk management and elaborates on Principle dealing with supervisory powers. Dearth of skilled human resources, poor financial strength of supervisor and consequent inability to retain talented staff, inadequate autonomy and the need for greater understanding of modern risk management techniques are identified as the main difficulties in quality implementation. The critical elements of infrastructure, legal framework that supports sound banking supervision and a credit culture that supports lending practices are the essence of a strong banking system. Widespread failures have occurred during a period of increased vulnerability that can be traced back to some regime change induced by policy or by external conditions.

Patrick Honohan explains the use of budgetary funds to help restructure a large failed Bank/Banking system and the various consequences associated with it. The article discusses how instruments can best be designed to restore Bank capital, liquidity and incentives. It considers how recapitalisation can be modeled to ensure right incentives for new operators/managers to operate in a prudent manner ensuring good subsequent performance. It discusses how
Government's budget and the interest of the tax payer can be protected and suggest that monetary policy should respond to the recapitalisation rather determine its design.

The author proposes the following four distinct policy tools to achieve four distinct goals—injecting assets, adjusting capital claims on the Banks, rebalancing the govt's own debt management and managing monetary policy instruments to maintain stability. The author also assessed the effect of bank recapitalisation for budget and debt management and implications for monetary policy and macro-economic environment in his article.

**Jacques de Larosiere**, former Managing Director of the International Monetary Fund discusses the implications of the new Prudential Framework. He explains at length how the new Regulatory code could have some dangerous side effects. The increased capital requirements as decided by the Basel Committee on Banking Supervision in September 2010 will affect the amount of own funds would affect the profitability of the Banks. The consequences of such increased capital requirements would incentivise the Banks to transfer certain operations that are heavily taxed in terms of capital requirements to shadow Banking to avoid the scope of regulation. The risks of such a practice might affect the financial stability. While the Central Banking authorities might contemplate registration and supervision of such shadow banking entities like the hedge funds and other pools, such a course might be more cumbersome than expected. The new regulation would result in the Banks to reduce activities with rather poor margins. For example they may reduce exposure to small and medium enterprises or increase credit costs or concentrate on more profitable but higher risk activities. He is also critical of the proposal of Basel to introduce an absolute leverage ratio that might push Banks to concentrate their assets in riskier operations. The author feels that the banking model which favours financial
stability and economic growth might become the victim of the new prudential framework, and force Banks to search for assets with maximum returns despite the attendant risks.

William Allen (2010) of Cass Business School, City University London strongly criticises the Basel Committee on Banking Supervision announcement increasing the capital requirements as part of Basel III. The aims of increasing the capital are two-fold. Firstly the objective is to increase the amount of liquid assets held by Banks and reduce their reliance on short term funding. It also aims at limiting the extent to which Banks can achieve maturity transformation. This focus on liability management, as per him will prove counterproductive, as has been proved historically by the recent financial crisis. As a strategy to meet the new Capital Accord Banks will be forced to amass large amounts of liquid assets, in addition to the amounts they will need to repay special facilities provided by the Governments and Central Banks. The liquidity coverage ratio envisaged in the Accord also will require Banks to hold 100% liquid asset coverage against liquidity commitments, and this will seriously impair the profitability of the Banks. The eligible liquid assets for this purpose will be predominantly Govt. Securities. This might motivate Governments to rely on this cheaper credit and some Governments may resort to abuse of this credit, thus creating a moral hazard. If a Government loses its creditworthiness, this will become 0% for Basel II purposes thus putting the Banks to a sudden jerk as the Securities would become ineligible as liquid assets. The author goes on to explain the conflict of interest of the members of the Basel Committee as some times these members are influenced by the Governments and their recommendations might not be taken as independent judgment.

Thus the author thinks that this regulation is seriously defective. He opines that this serious lacuna could be removed by enlarging the opportunities for liquid assets to be created out of the
Bank’s claims on the private sector as well. As per him, Commercial Bills could be considered to be eligible for this purpose as they are self liquidating transactions. As commercial Bills are accepted by Banks, it is less likely that they will be in default. The cardinal point in liquidity management to be remembered is that Commercial Banks cannot aim at zero risk. In that case they would need to their assets in currency and would have to charge their customers for accepting deposits. The solution is not to aim thoughtlessly at excessive liquidity, but in putting in place Robust Risk Management practices.

Abel Mateus (2010) which appeared also in the IUP Journal of Banking & Insurance Law, Vol.VIII, Nos.1 & 2, 2010 made a thorough study of the Regulatory reform requirements in the modern context after the global meltdown. He starts by summarizing the basic principles that should be covered in the financial reforms. He reviews the progress achieved by the Financial Stability Board (FSB) and Basel Committee on Banking Supervision. He discusses the unresolved issues like the relationship between competition policy and financial stabilization policies. He throws particular light on the oft quoted Too-Big-To-Fail’ (TBTF) concept. He outlines measures to improve the supervision of capital markets to protect consumers and Investors. The articles discusses at length the revision of Bank Capital Requirements and Accounting Procedures, revising the role of Credit Rating Agencies, the supervision and regulation of Hedge Funds, Commodity Funds and Private Equity Funds. Complex issues of Derivatives Regulation, Mortgage Securitization etc. Have also been discussed and the author came out with suggested methods to address these difficult issues.

The LSE Report of the London School of Economics and Political Sciences is a very important document in analysing the role of finance in the build-up to the recent crisis. The tax bail - bail-
outs have been criticised and the gradual increase in the equity financing would shift the responsibility of any crisis towards the shareholders. As per Peter Boone and Simon Johnson, the global financial system is facing grave risks due to the bail-out policy of the Western Governments. As Regulatory bodies like the Central Banks are keen to increase the degree of oversight, the Banks would create new loopholes. The authors opine that in the absence of any international treaty for the regulation of global financial institutions, macro prudential measures and proper Risk Management systems are necessary for the management of financial system. As per Goodhart the cost of Bank failures can be very large which lends justification to impose tighter supervisory and regulatory measures. He argues that the proposals under the Basel III to increase the capital higher levels like 20-30% are very justified. This is strongly objected by Laurence Kotlikoff who feels such higher levels of capital would penalise the Shareholders and Depositors and goes against the very principle that Financial Institutions are agencies which should have the benefits of gearing.

**Bessone, Biagio (2000)** feels that Banks are special as they not only accept and deploy large amounts of uncollateralised public funds in a fiduciary capacity, but also leverage such funds through credit creation. Thus Banks have a fiduciary responsibility. Banks play a crucial role in deploying funds mobilized through deposits for financing economic activity and providing the lifeline for the payments system. A well regulated Banking System is very central to the country's economy. The author examines the way Banking and other financial institutions interact with each other during different stages of economic development. As per the author the shareholders of the banks who are supposedly owners have only a minor stake and the considerable leveraging capacity of banks put them in control of very large volume of public
funds, though their actual stake may be very limited say sometimes only ten per cent or even lower. The author feels that in the light of this leveraging capacity, the Banks should act as trustees. The author underlines the need for the Supervisors and Regulators of the country's Banking system to discharge the onerous responsibility of ensuring that the Bank Managements fulfill this fiduciary relationship well, as in a developing economy there is far less tolerance for downside risks among depositors, many of whom place their life savings in the Banks. The author feels that diversification of ownership is desirable as the risk of concentration of ownership can lead to moral hazard problem and linkages of owners with businesses. When the ownership is diversified there is greater need for corporate governance and professional management in order to safeguard the depositors' interest and ensure systemic stability. Hence the regulatory and supervisory framework has to ensure that banks follow prudent and transparent accounting practices and are managed in accordance with the best practices for risk management.

As per G.Dalai, D.Rutherberg, M.Sarnat and B.Z.Schreiber (1997) Risk is intrinsic to banking. However the management of risk has gained prominence in view of the growing sophistication of banking operations, derivatives trading, securities underwriting and corporate advisory business etc. Risks have also increased on account of the on-line electronic banking, provision of bill presentation and payment services etc. The major risks faced by financial institutions are of course credit risk, interest rate risk, foreign exchange risk and liquidity risk.

Credit risk management requires that Banks develop loan assessment policies and administration of loan portfolio, fixing prudential per borrower, per group limits etc. The tendency for excessive dependence on collateral should also be looked into. The other weaknesses in Credit Risk
Management are inadequate risk pricing, absence of loan review mechanism and post sanction surveillance.

Interest rate risk arises due to changes in interest rates significantly impacting the net interest income, mismatches between the time when interest rates on asset and liability are reset etc. Management of interest rate risk involves employing methods like Value-at-Risk (VaR), a standard approach to assess potential loss that could crystallise on trading portfolio due to variations in market interest rates and prices. Foreign Exchange risk is due to running open positions. The risk of open positions of late has increased due to wide variations in exchange risks. The Board of Directors should lay down strict intra-day and overnight positions to ensure that the Foreign Exchange risk is under control.

Chief Risk Officer, Alden Toeys (2011) of Commonwealth Bank of Australia states that a major failure of risk management highlighted by the global financial crisis was the inability of financial institutions to view risk on a holistic basis. The global financial crisis exposed, with chilling clarity, the dangers of thinking in silos, particularly where risk management is concerned' says the author. The malady is due to the Banks focussing on individual risk exposures without taking into consideration the broader picture. As per the author the root of the problem is the failure of the Banks to consider risks on an enterprise-wide basis. The new relevance and urgency for implementing the Enterprise Risk Management (ERM) is due to the regulatory insistence with a number of proposals to ensure that institutions stay focussed on the big picture. In a way the Three Pillar Approach frame work of the Basel II Accord is an effort to fulfill this requirement. The risk weighted approaches to Credit Risk on the basis of the asset quality, allocation of
capital to Operational Risk and Market Risks nearly capture all the risks attendant to a Bank's functioning.

**Chapelle, Crama, Hubner and Peters (2008)** examine the use of the advanced measurement approach (AMA) for the measurement of operational risk for firms within Europe. Two business lines: asset management and retail banking, and two event types: expected losses and unexpected losses of a large financial institution are used for the test basis. The results suggest that there can be substantial savings with the utilization of AMA.

**Shafiq and Nasr (2009)** examine the risk management practices followed by commercial banks in Pakistan. The results reveal the following: (i) the greatest exposures banks face are credit risk, liquidity risk, interest rate risk, foreign exchange risk and operating risk; (ii) significant differences exist in the application of risk management practices among public sector and local private commercial banks; and (iii) commercial banks’ staff basically understand risk management but additional training is required to enhance their expertise in the area.

### 2.3 LITERATURE REVIEW: INDIAN PERSPECTIVE

**Rekha Arunkumar and Koteshwar (2006)** feel that the Credit Risk is the oldest and biggest risk that Banks, by virtue of their very nature of business inherit. The pre-dominance of credit risk is the main component in the capital allocation. As per their estimate credit risk takes the major part of the Risk Management apparatus accounting for over 70 per cent of all Risks. As
per them the Market Risk and Operational Risk are important, but more attention needs to be paid to the Credit Risk Management in Banks.

**Reserve Bank of India, Volume 3, 1967-81** gives very valuable account of the evolution of Central Banking in India. This third volume describes vividly the background against which the Reserve Bank of India came into being on April 1, 1935. Before the establishment of the Reserve Bank, the Central Banking functions were handled by the Imperial Bank of India. The Royal Commission on Indian Currency and Finance (Hilton Young Commission) 1926 recommended that there is conflict of interest in the Imperial Bank of India functioning as the controller of currency while also functioning as a Commercial Bank. After detailed analysis on the ownership, constitution and composition of the ownership, RBI was established by a Bill in the Legislative Assembly. It was in 1948 that the Reserve Bank of India was nationalised under the RBI(Transfer to Public Ownership) Act, 1948. The earlier volumes viz., Volume I and Volume II covered the developments in Central Banking up to 1967. Volume III covers the period 1967 to 1981. This is the most dynamic period in the history of Commercial Banking. The Government was very critical of the attitudes of the Private Banks for their failure to be socially responsible, which led the Govt. To impose social control on Banks. Mrs. Indira Gandhi nationalised 14 Banks during July 1969. Reserve Bank was given newer responsibilities in terms of the Developmental role.

The RBI was assigned not only the role of maintaining monetary and fiscal stability but also the developmental role of establishing institutional framework to complement commercial banking to help agriculture, SSI and Export Sectors. RBI, despite the criticism of not enjoying adequate
autonomy due to the interference of the Finance Ministry (with Govt. Ownership of most Banking Companies) has been able to commendably discharge the regulatory functions. True it was during this period that the performance of the Indian Banks deteriorated with most Nationalised Banks wiping out their capital and their Balance Sheets showing huge negativities in terms of quality of assets etc.


**S.K.Bagchi (2005)** observed that in the world of finance more specifically in Banking, Credit Risk is the most predominant risk in Banking and occupies roughly 90-95 per cent of risk segment. The remaining fraction is on account of Market Risk, Operations Risk etc. He feels that so much of concern on operational risk is misplaced. As per him, it may be just one to two per cent of Bank's risk. For this small fraction, instituting an elaborate mechanism may be unwarranted. A well laid out Risk Management System should give its best attention to Credit Risk and Market Risk. In instituting the Risk Management apparatus, Banks seem to be giving equal priority to these three Risks viz., Credit Risk, Operational Risk and Market Risk. This may prove counter-productive.
Securitization and Reconstruction of Financial Assets Enactment of Security Interest Act, 2002. (SARFAESI ACT). Govt. Of India has taken the initiative of making the legislation to help Banks to provide better Risk Management for their asset portfolio. Risk Management of the Loan book has been posing a challenge to the Banks and Financial Institutions which are helpless in view of the protracted legal processes. The act enables Banks to realise their dues without intervention of Courts and Tribunals. As a part of the Risk Management strategies, Banks can set up Asset Management Companies (AMC) to acquire Non Performing Assets of Banks and Financial agencies by paying the consideration in the form of Debentures, Bonds etc. This relieves the Bank transferring the asset to concentrate on their loan book to secure that the quality of the portfolio does not deteriorate. The act contains severe penalties on the debtors. The AMC is vested with the power of issuing notices to the Borrowers calling for repayment within 60 days. If the borrower fails to meet the commitment, the AMC can take possession of the secured assets and appoint any Agency to manage the secured assets. Borrowers are given the option of appealing to the Debt Tribunal, but only after paying 75% of the amount claimed by the AMC. There are strict provisions of penalties for offences or default by the securitisation or reconstruction company. In case of default in registration of transactions, the company officials would be fined upto Rs.5,000/- per day. Similarly non-compliance of the RBI directions also attract fine up to Rs.5 lakhs and additional fine of Rs.10,000/- per day. This has proved to be a very effective Risk Management Tool in the hands of the Banks.

The Report of the Banking Commission 1972 - RBI Mumbai. The Commission made several recommendations for making the Indian Banking system healthier. The commission observed that the system of controls and supervisory oversight were lax and underlined the need for
closure supervision of Banks to avoid Bank failures. However most of the recommendations of the Commission lost their relevance in view of the priorities of the Government which is more concerned with its political compulsions. The nationalisation of Banks and the tight control on the Banks of the Govt. Left little scope for implementation of the recommendations of the Commission. If only the recommendations which are meant to restore tighter regulatory measures, strengthening of the internal control systems and professionalization of the Bank Boards were properly appreciated and implementation, Indian Banks would not have ended in the mess of erosion of capital, mounting burden of non-performing assets etc.

A well known study analysing the performance of Commercial Banks in India was conducted by [Avtar Krishna Vashist (1991)](1991): Public Sector Banks in India - H.K.Publishers & Distributors, New Delhi 1991. In order to find out relative performance of different Banks, composite weighted growth index, relative growth index and average growth index of Banks were constructed. The study revealed that Commercial Banks did well with respect to Branch expansion, deposit mobilisation and deployment of credit to the Priority Sectors. But they showed poor performance in terms of profitability. After identifying the causes of the decline in profitability a number of suggestions were made to improve the performance of Commercial Banks in the Country.

[Dr.Atul Mehrotra, Dean, Vishwakarma Institute of Management (2011)] emphasises the need for promotion of Corporate Governance in Banks in these uncertain and risky times. This paper discussed at length Corporate Governance related aspects in Banks as also touches upon the principles for enhancing Corporate Governance in Banks as suggested by BCBS. The author felt that despite the RBI's initiatives on the recommendations of the Consultative Group of
Directors of Banks/Financial Institutions under the Chairmanship of Dr. A.S. Ganguly, member of the Board for Financial Supervision, there is more ground to be covered before Indian Banks are in a position to attain good Governance Standards. As per the author he Public Sector Banks with Government ownership control almost over 80 per cent of banking business in India. This complicates the role of the Reserve Bank of India as the regulator of the financial system. The role of the Government performing simultaneously multiple functions such as the manager, owner, quasi-regulator and sometimes even as super-regulator presents difficulties in the matter. Unless there is clarity in the role of the Government, and unless Boards of the banks are given the desired level of autonomy, it will be difficult to set up healthy governance standards in the Banks.

As a part of the Review of literature, the Reports of various Committees and Commissions have been perused. Important among them are given below:

The Report of the Committee on the Financial System 1991 Chairman Shri M.Narasimham (1991) by far is the most important document while discussing the Reform process in Indian Banking. The following recommendations made by the Committee which were largely implemented put the Indian Banking system on an even keel:

Main Recommendations:
1. Operational flexibility and functional autonomy
2. Pre-emption of lendable resources to be stopped by progressively reducing the SLR and CRR
3. Phasing out of directed Credit Programmes
4. Deregulation of interest rates

5. Capital Adequacy requirements to be gradually stepped up

6. Stricter Income Recognition norms

7. Provisioning requirements tightened

8. Structural Organisation

   a) Three to four Large Banks (including State Bank of India) which could become international in character;

   b) Eight to ten national banks with a network of branches throughout the country engaged in 'universal' banking;

   c) Local Banks whose operations would be generally confined to a specific region;

   d) Rural Banks including Regional Rural Banks confined to rural areas.

9) Level playing field for Public Sector and Private Sector Banks

10) No further nationalization

11) Entry of Private Sector Banks recommended

12) Banks required to take effective steps to improve operational efficiency through computerization, better internal control systems etc.

Committee on Banking Sector Reforms (1998) - Chairman Shri M.Narasimham (popularly known as Narasimham Committee II) Report discusses the steps required for further strengthening the Banking system by concentrating on prudential management, introduction of technology etc. The main recommendations of the committee are:

1. Capital Adequacy norms further tightened to include market risk in addition to credit risk

2. Capital requirement for foreign exchange open positions

3. Capital adequacy to be increased to 10 per cent in a phased manner
4. Further tightening of prudential norms

5. Ever greening of assets to be detected and errant Banks punished

6. No recapitalization from the Govt. Budgets

7. Transfer of Assets to Asset Reconstruction Co.

8. Introduction of Tier II Capital

9. Asset/Liability Management: Risk Management

10. Internal Systems

11. Human Resources Management

12. Technology Up gradation

The Report laid emphasis on the strengthening of regulatory measures and implement Risk Management strategies to secure the soundness of Banks.

As per Dr.Rakesh Mohan, Deputy Governor, Reserve Bank of India (2004) he objective of reforms in general was to accelerate the growth momentum of the economy defined in terms of per capital income.

The quality of functioning of the financial sector can be expected to effect the functioning and productivity of all sectors of the economy. He discusses at length the role of the Banking Sector and its influence over the rest of the economy. As per him, the transformation of the Banking sector in India needs to be viewed in the light of the overall economic reforms process along with the rapid changes that have been taking place in the global environment within which the Banks operate. The global forces of change include technological innovation, the deregulation of financial services internationally, our own increasing exposure to international competition and equally important, changes in corporate behaviour such as growing disintermediation and
increasing emphasis on shareholder value. He cites the examples of recent banking crises in Asia, Latin America and elsewhere having accentuated these pressures.

India embarked on a strategy of economic reforms in the wake of a serious balance of payments crisis in 1991. The main plank of the reforms was reform in the financial sector, with banks being the mainstay of financial intermediation, the Banking Sector. The main purpose of the reform process was aimed at promoting a diversified, efficient and competitive financial system with the ultimate objective of improving the allocative efficiency of resources through operational flexibility, improved financial viability and institutional strengthening.

**Dr. Y. V. Reddy (2005), Governor, Reserve Bank of India** observed that the Indian financial system in the pre-reform period (i.e., prior to Gulf Crisis on 1991) was preoccupied with fulfilling the financial needs of the Planning process to the neglect of the health of the Banks. Due to Government's dominance of ownership of Banks, large scale pre-emptions in terms of Statutory Liquidity Ratio and Cash Reserve Ratio were resorted to and the Banks' Managements fell short of their professional attitude with the result they functioned at the behest of the Finance Ministry. As per him the Reform process has created an enabling environment for Banks to overcome the constraints faced by them. For example deregulation of interest rates, bringing down the pre-emptions viz., Statutory Liquidity Ratio and Cash Reserve ratio to workable levels in a phased manner, dispensing with the system of directed lending have helped Banks in restoring their financial health. The reserve Bank has initiated several changes in their prudential oversight on Banks laying more emphasis on improving the asset quality and earning. The changes brought about in terms of ownership of Banks also had a salutary effect on the working of the Banks. The share of the public sector banks in the aggregate assets of the Banking Sector
which was 90 per cent in 1991 has gradually come down and by 2004 the same was around 75 per cent. He opined that as a result of the various measures taken as a part of the Reforms, the Reserve Bank has been able to ensure overall efficiency and stability of the Banking System in India. The capital adequacy of Indian Banks now is comparable to those at international levels. The asset quality of the Banks has registered marked improvement. The Non-Performing Assets to Gross advances for the Banking system have reduced from 14.4 per cent in 1998 to 7.2 per cent in 2004. The return on assets (ROA) was at a low of 0.4 per cent in the year 1991-92. By 2003-04 it has improved to 1.2 per cent. In his concluding observations he expressed that consolidation, competition and Risk Management are critical to the future of the Banking system. Equally governance and financial inclusion also have to be given top priority.

**Mrudul Gokhale (2009)** elaborately dealt with the subject of capital adequacy in Banks. As per her Banks mostly give adequate focus for the credit risk aspect. There is a shift from the qualitative risk assessment to the quantitative management of risk. In tune with the regulatory insistence on capturing risks for the purpose of capital charge, sophisticated risk models are being developed. These models help Banks to near accurately quantify the potential losses arising from different risks viz., credit risk, market risk and operations risk. This will enable the Regulator to ascertain whether individual Bank has accurately compiled the risk profile of assets.

As per them the Banking system is central to a nation’s economy and Banks are special as they not only accept and deploy large amounts of uncollateralised public funds in a fiduciary capacity, but also leverage such funds through credit creation. They argue that large industries and big business houses enjoyed major portion of the credit facilities to the neglect of Agriculture, small-scale industries and exports. In fact the main inspiration for nationalisation was the larger social purpose. The nationalisation in two phases (14 banks in 1969 and 6 more in 1980). Since nationalisation Banking system played pivotal role in the Indian economy, acting as an instrument of social and economic change. They quote Tandon 1989: "Many bank failures and crises over two centuries, and the damage they did under laissez faire conditions, the needs of planned growth and equitable distribution of credit which in privately owned banks was concentrated mainly on the controlling industrial houses and influential borrowers, the needs of growing small scale industry and farming regarding finance, equipment in inputs.; from all these there emerged an inexorable demand for banking legislation, some government control and a central banking authority, adding up, in the final analysis, to social control and nationalisation"

Nationalisation resulted in several advantages to the economy. There was stupendous growth in volumes. Banking network has spread to rural and hitherto uncovered areas. However, the nature of ownership of Banks subjugated them to the control of the Government. There was very little autonomy due to the fact that both lending and deposit rates were regulated until the 1980's. There was complete lack of competition and this has resulted in overall inefficiency and low productivity. All the disadvantages of a monopolistic regime were in play.

As per them the reasons for this sad state of affairs prior to the reform process were:

- High reserve requirements
• Administered interest rates

• Directed credit and

• Lack of competition

• Political interference and corruption

As per the paper the recommendations of the Narasimham Committee Report (1991) brought about the required changes to restore autonomy to Banks. Among the measures introduced reduction of reserve requirements, de-regulation of interest rates, introduction of prudential norms, strengthening of Bank supervision and improving the competitiveness of the system, particularly by allowing entry of private sector Banks were the most important. The authors make a reference to the Basel Committee (1988) framework on capital adequacy norms. They feel that the efforts of the Reserve Bank of India in directing the Banks to maintain risk-weighted capital adequacy ratio initially at the lower level of 4 per cent and subsequently raising it to 9 per cent were timely with a view to bringing about parity for Indian Banks with international best practices.

As per the authors the period 1992-97 laid the foundations for reforms in the Banking system (Rangarajan, 1998). References were made to the Second Narasimham Committee Report (1998) which focussed on issues like strengthening of the Banking system, upgrading of technology and human resources development. "The report laid emphasis on two aspects of Banking regulation viz., capital adequacy and asset classification and resolution of NPA-related problems".

The paper covered a period of 25 years (period from 1981 to 2005) The study was based on the following indicators:
• Number of banks and offices
• Deposits and credit
• Investments
• Capital to risk-weighted assets ratio (CRAR)
• Nonperforming assets (NPAS)
• Income composition
• Expenditure composition
• Return on Assets (ROAS) and
• Some select Ratios.

The study leads to very important revelations. As per the study there has been a spurt in the number of banks during the late 1990s, which decreased during the early period of the new millennium. The authors feel that this could be due to the consolidation process and in particular, the mergers and acquisitions that are the order of the banking system at present. After the consolidation phase during the late 1980s and early 1990s, there has been a moderate.

V.Subbulaxmi and Reshma Abraha (2006) discuss the common causes of crises and their impact on the economic conditions. Banking crises may lead to rapid change in the environment in which the Bank operates. Sooner the restructuring programme is initiated, the faster the recovery and the lower the cost of recovery. The two fundamental objectives behind every resolution programme are:

1) Restoration of the functioning of the payments system and

2) Minimisation of the public funds used in the restructuring process
The authors discuss the various options of resolution available depending on the intensity and the cause of the crises. As there is no single medicine that would cure the problem an analytical approach is suggested to deal with the crises situations.

Addresses of the Governors of the Reserve Bank of India at various conventions and For a provide valuable insights into the Regulators views on the Reform Process. SICOM Silver Jubilee Memorial Lecture delivered by Mr. C. Rangarajan in 1998 at Mumbai gave a graphic account of the maladies of the Indian Banking System and also outlined measures to be taken for their better working. Most of his observations dealt with the financial health of the Banks and the underlying need to bring the Indian Banks on par with international standards.

Dr. Y. V. Reddy (2003) presented Papers at World Bank International Monetary Fund and Brookings Institution Conference on Financial Sector Governance, The roles of Public and Private Sectors, Public Sector Banks and the Governance Challenge: Indian Experience, Monetary and Financial Sector Reforms in India: A Practitioner's Perspective (Indian Economy Conference, Cornell University, USA (2003), Towards Globalisation in the Financial Sector in India' - Inaugural address at the Twenty Fifth Bank Economists Conference, Mumbai. In these addresses Dr. Reddy discussed the various initiatives being taken by the Reserve Bank of India to ensure financial health of the Banks. The regulatory changes initiated by the Reserve Bank of India, the shift from micro-prudential regulation to macro regulation have been discussed. The changes initiated have brought about a sea change in the ownership of the Banks, a marked improvement in the soundness parameters like the return on assets, staff productivity, technology, asset quality etc.
Mr. G. Ramathilagam and Ms. S. Preeth (2007) attempted to evaluate the cost efficiency of Indian Commercial Banks during the post reform period. They used data for 10 years from 1992. They found that during the post reform period Banks have improved their cost efficiency by as much as 10 per cent. They suggested that Banks have to be more cost conscious. As per them the Banks Auditors and internal audit machinery do not attach much importance to the cost aspects. There is no proper utilization of the resources of the Bank resulting in under utilisation of the same.

However, the authors do not agree to the popular notion that Bank staff is less productive and do not feel that Banks are overstaffed. This view of the authors is in total disagreement with even the Industry Circle and the Government who feel that a lot of scope exists to make the Bank staff in India to be more productive which would improve financial performance of Banks. For example, the per employee contribution in terms of Deposits and Advances needs improvement, which would result in substantial increase in profitability of Banks.

Ms. M. Banumathu (2005) the author attempts a comparison between Banks which are adequately capitalized and Banks which are under capitalized. She used a set of 14 financial ratios for her analysis. She came to the conclusion that Banks which are adequately capitalized performed better with lower operating costs and higher returns on equity. However, her excessive reliance only on capitalization renders her analysis somewhat short sighted as a number of other factors like the efficiency of the Management, the Banks culture in terms of subjecting the available capital to optimum use, staff productivity etc. are important factors which were not considered by the author.
Reserve Bank of India, Guidelines for implementation of the New Capital Adequacy Framework (2003) form an important step in ensuring that the Indian Banks are adequately capitalised as per the prescriptions of the Basle Committee on Banking Supervision (BCBS). It was in April 1992 that the Reserve Bank of India introduced a risk asset ratio system for all banks including foreign Banks in India as a capital adequacy measure. As per this system, the balance sheet assets both funded and non-funded items and other off-balance sheet exposures are assigned prescribed risk weighs. Banks were required to maintain unimpaired minimum capital funds equivalent to the prescribed ratio on the aggregate of the risk weighted assets. BCBS released the 'International Convergence of Capital Measurement and Capital Standards: A Revised Framework' on June 26, 2004. The revised Framework consists of three-mutually reinforcing Pillars, viz., minimum capital requirements, supervisory review of capital adequacy and market discipline. The core of the Basel Accord is its risk sensitivity approach. The Accord offers three distinct options for computing capital requirement for credit risk and three other options for computing capital requirement for operational risk. The options available for computing capital for credit risk are on the basis of Standardised Approach, Foundation Internal Rating Based Approach and Advanced Internal Rating Based approach. The options available for computing capital for operational risk are Basic Indicator Approach, Standardized Approach and Advanced Measure Approach. The reserve bank advised Banks to maintain a minimum capital adequacy of 9 per cent as against the BCBC prescription of 8 per cent. Capital funds are treated as Tier I and Tier II capital. Tier I is the core capital consisting of paid-up equity capital, statutory reserves and other disclosed free reserves if any. Certain other items like capital reserves, and items notified by the RBI for inclusion in Tier I may be treated as Tier I capital. Items included in Tier II capital are items like Revaluation Reserves, General Provisions
and Loss Reserves, Hybrid debt capital instruments and Subordinated Debt. The Reserve Bank required Banks to reach a minimum Tier I CRAR (Capital to Risk Weighted Assets Ratio) of 6%, as against the BCBS requirement of only 4 per cent.

The Core Principles for Effective Banking Supervision released by the BCBS in 1997 stated that the Banking supervisors must be satisfied that the Banks under their jurisdiction have adequate policies and procedures for identifying, monitoring and controlling country risk and transfer risk in the international lending and investment activities and for maintaining reserves against such risks (Principle XI). The Reserve Bank reviewed the position in India in the light of this and found that Country Risk Management (CRM) was one area where there was an observed deficiency in the India Banks. Hence the RBI has initiated steps to elicit the views of the Banks on the basis of the Draft Guidelines and issued final Guidelines in February 2003. These guidelines were made applicable to countries where an Indian Bank has more than 2 per cent or more of its assets. The guidelines are fairly detailed in nature with policy and procedures. The RBI wanted the Banks to follow a rigorous CRM policy and implement the 'Know Your Customer' (KYC) guidelines strictly in their International activities. RBI further defined the scope of these guidelines to include both funded and non-funded exposures from their domestic as well as foreign branches for the purpose of identifying, measuring, monitoring and controlling country risks. Funded exposures include Cash and bank balances, deposit placements, investments, loans and advances and non-funded exposures include letters of credit, guarantees, performance bonds, bid bonds, warranties, committed lines of credit etc. The guidelines suggest that the Banks Boards must set suitable Country Exposure Limits as a part of their Risk Management Policy and constantly monitor that such limits are respected by the field level
functionaries. The guidelines also cover Provisioning and Disclosure requirements for all International Exposures of Banks.

**Reserve Bank of India "Corporate Debt Restructuring (www.rbi.org.in)"** is a major initiative of the Reserve Bank of India in helping the Banks to cope with the mounting burden of Non-Performing Assets is the announcement of Corporate Debt Restructuring (CDR). The objective of CDR is to ensure a timely and transparent mechanism for restructuring of the Corporate Debts. The scheme is applicable only for viable Corporates which are affected by internal and external factors and which are outside the purview of the Board for Industrial and Financial Restructuring (BIFR), Debt Recovery Tribunals (DRTs) or other legal proceedings. The process of CDR mechanism is to reschedule the debt portfolio of the borrowers to help them in the revival of projects and continue operations through reductions in existing debt burden and establish new credit lines. This would help the lender to reduce the risk in risk to optimize the returns. RBI prescribed three tier structure viz., CDR Standing Forum, CDR Empowered Group and CDR Cell. The CDR Cell would function as the Secretariat for the CDR Standing Committee and CDR Empowered Cells. The CDR Empowered Group is required to look into each case of debt restructuring, examine the viability and rehabilitation potential of the company and approve the proposal within a time frame of 90 days. In exceptional cases the time limit may be extended up to 180 days. The Scheme is applicable to standard and sub-standard accounts and potential cases of Non-Performing-Assets would get a priority in disposal. CDR mechanism is applicable to exposures of Rs.20 crores and above involving more than one Bank in the form of syndication/consortium arrangement.
Reserve Bank of India, Mumbai (June, 2001) "Report of the Advisory Group on Banking Supervision" The Committee on Banking Supervision, more popularly known as the Verma Committee was appointed to study the present status of applicability and relevance and compliance in India of the standards and codes. The Committee was asked to recommend measures to chalk out a course of action for achieving the international best practices. The Group made a thorough study of the following areas:

- Corporate Governance
- Internal Control
- Risk Management
- Loan Accounting
- Transparency and disclosures
- Financial Conglomerates and
- Cross-Border Banking Supervision

The Committee felt that given the level of complexity and development of the Indian Banking Sector, the level of compliance with the standards and codes is of a high order. Where there are significant gaps the committee recommended that necessary amendments to laws are put in place without delay. On Corporate Governance the Committee felt that the nature of ownership of Banks in India sometimes leads to confusion. As per the Committee the predominant Government ownership of Banks leads to the dilution of standards of Governance. The Committee is of the view that irrespective of the ownership pattern, the quality of Corporate Governance should be the same.

On Risk Management, the Group recommended greater orientation of the bank's managements and their boards towards better understanding of the risks and their management. The Group felt
that the better equipped and more capable Banks should take the initiative and act as forerunners so that they could act as models for other Banks to follow.

The other areas where the Committee made important recommendations are Management Information System (MIS), Internal Controls and Compliance, Transparency and Disclosures, Supervision of Conglomerates and Cross-Border Banking Supervision.

Mr. P. Kallu Rao (2010) states that the birth place for the current financial crisis is the United States, where the Banking system created the sub-prime crisis in 2007. The contagion effect was felt in many countries. The crisis has affected in two ways viz., financial contagion and spill-overs extending to securities markets and economic slowdown which resulted in changing perceptions about trade practices, foreign direct investment etc. This paper deals at length various issues in identification of risk and its management. The paper suggests measures to minimize the spread of financial contagion and to reach financial stability. The article highlights the agenda for financial sector policy making including financial innovation and the need for reviewing the financial sector regulations.

Thirupathi Kanchu and M. Manojkumar (2013) have concluded in their paper that Risk management underscores the fact that the survival of an organization depends heavily on its capabilities to anticipate and prepare for the change rather than just waiting for the change and react to it. The objective of risk management is not to prohibit or prevent risk taking activity, but to ensure that the risks are consciously taken with full knowledge, clear purpose and understanding so that it can be measured and mitigated. Functions of risk management should actually be bank specific dictated by the size and quality of balance
sheet, complexity of functions, technical/professional manpower and the status of MIS in place in that bank. Risk Management Committee, Credit Policy Committee, Asset Liability Committee, etc are such committees that handle the risk management aspects. The banks can take risk more consciously, anticipates adverse changes and hedges accordingly; it becomes a source of competitive advantage, as it can offer its products at a better price than its competitors. Regarding use of risk management techniques, it is found that internal rating system and risk adjusted rate of return on capital are important. The effectiveness of risk measurement in banks depends on efficient Management Information System, computerization and networking of the branch activities.

Kulwant Pathania and Sabina Batra, (2008) has made a study on “NPA Management in cooperative Banks: Perceptions of Bank Officials” and has observed that the committee on Non-Performing Assets of Public Sector Banks (1998) rightly observed that NPA is a double-edged knife that tells on a bank’s profitability. On one hand, banks cannot recognize income (interest) on NPA accounts and on the other, it is a drain on bank’s profitability due to funding cost’. The Narasimhan Committee Report 1998 rightly pointed out that NPA constitute a real economic cause to the nation in that they reflect the application of scarce capital and credit funds to unproductive uses. The money locked up in NPAs is not available for productive use and to the extent that the banks seek to make provision for NPAs, it is charge on the profit’. High NPAs in the banks have devastating effects not only on the banks but also on the economy as a whole’. The formulation of the good policy will be of no use unless it is implemented in true spirit.
Dr. Gurcharan Singh and Sukhmani (2011) studied on “An Analytical Study of Productivity and Profitability of District Central Cooperative Banks in Punjab” focused on evaluating performance of cooperative banks in the state of Punjab. Six District Central Cooperation Bank (DCCBs) from the state of Punjab has been selected for the study. Their productivity and profitability have been studied for a period of nine years (1999-2000). It is found that profitability in all selected DCCBs of Punjab had shown a negative trend whereas the productivity improved significantly over the period of study.

Dr. Mrs. Ratna and K. Nimbalkar (2011) analyzed on “A Study of NPA” -Reference to Urban Co-Operative Bank” Focused On urban co-operative banks facing keen competition with public sector banks and private sector banks, particularly after globalization in 1991. At the same time these banks are facing the problem of Non-Performing Assets also.