

K C Chakrabarty: Challenges for next generation banking

Address by Dr K C Chakrabarty, Deputy Governor of the Reserve Bank of India, at the Indian Chamber of Commerce and Industry, Coimbatore, 25 June 2011.

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Mr. Krishnan, President of Indian Chamber of Commerce and Industry, Coimbatore; Mr. M. Narendra, Chairman and Managing Director of Indian Overseas Bank; Mr. D. Raj Kumar, Regional General Manager, The Hindu; Mr. K.G. Balakrishnan, Past President of ICCI, Coimbatore; members of ICCI and captains of industries in Coimbatore; representatives of banks in Coimbatore; members of the print and electronic media; distinguished invitees, ladies and gentlemen,

I am very happy to speak at this “Voice of Tomorrow – Fuel to Excel”, programme which is a commendable initiative by ICCI, Coimbatore and the Hindu.

At the outset we must be clear about whose voice we are talking about when we say voice of tomorrow. To my mind the voice tomorrow belongs to the youth and the millions of business entrepreneurs of the country. Not that the voice of business is not heard now. But they are by and large limited to lobbying through associations like ICCI. What I mean is that the collective voice of millions of private enterprise across the country. It is this voice together with the voice of the youth which will mould and build the future of this country.

The young demography of this country will make the voice of the youth matter the most, going forward. And in a market based economy, with further reforms in critical areas to follow, the private business community will increasingly shape the face of the economy and also become a prominent voice in setting our vision for the future. It is in this context that industrial cities like Coimbatore assume importance.

Mr. Narendra mentioned that the Indian economy is likely to register an average growth of above 8% in the Eleventh Five Year Plan and that the 12th Plan will see a growth of 9 to 10%. It is my view that it is possible for India to aim at a 10% growth for the next 20 years. Only then growth will be truly sustainable and inclusive. Private enterprise and investment coupled with the demographic advantage can be the underlying drivers of the country's immense growth potential, going forward. We cannot forget the fact that India's new growth trajectory of the last decade coincided with a significant pick up in private investment and a transition to a younger demography. Both factors make us believe now that a 10 per cent growth can be achieved and sustained, going forward.

At that rate, India's share in world GDP will rise from the current level of about 2 per cent to 10 per cent by 2030. But this will not happen by itself. Mere policy will not transform into growth. This will happen only when all of us work hard to overcome the challenges and seize the opportunities offered by global and domestic developments. Let me highlight some of the major challenges and opportunities.

Now, Mr. Narendra talked about the demographic dividend. India is the only country in the world where the working population would increase for the next 20 years. Young demography offers us an opportunity, but addressing the challenge of creating adequate productive employment opportunities will determine how best we are able to reap the demographic dividend. Estimates of United Nations suggest that by 2041, working age population in India will increase by 312 million, while in China it will decline by 126 million. Creating gainful employment for this order of new entrants to the labour market is a daunting challenge but not impossible.

Education and skill development are the challenges here. When I say education, what I mean is quality education. The demographic change will generate a huge scope for quality education but the demographic dividend can be reaped only if we can make quality

education affordable. I believe that technology and innovation can make such education accessible and affordable by bringing down the unit cost of quality education. It is here that places like Coimbatore, which is both a centre of educational and entrepreneurial excellence, can play a leading role.

We must accept the fact that the overall skill base of India is rather low compared to developed economies. This may be difficult to believe, given the global recognition our IT professionals have received and the well known contribution of this sector to the knowledge economy. I have often wondered why our talented youth can perform so well in Silicon Valley but fail to do so in their home country.

With services accounting for 65 percent of the country's GDP, one would tend to presume that India's growth must be skill intensive. Facts, however, suggest the opposite. Many developed countries have tertiary enrolment (*i.e.* vocational training) levels of 60 to 80 per cent in the age group of 15–29, which is as high as 96 per cent for Korea. The comparable level for India is less than 15 per cent. Expenditure on research and development (R&D) in the developed countries is in the range of 2 to 3 per cent of GDP on an average, which is just 0.8 per cent in India. This probably explains the gap between employment and employability in our country. How to bridge this gap is the challenge for the voice of tomorrow.

The skill gap will become increasingly costly for the economy. Way back in 1948, while addressing the conference on All India Education, Maulana Azad had stressed that "...we must not for a moment forget, it is a birth right of every individual to receive at least the basic education without which he cannot fully discharge his duties as a citizen". In April 2010, on the occasion of "The Children's Right to Free and Compulsory Education Act" becoming effective, the Hon'ble Prime Minister emphasized: "...We are committed to ensuring that all children, irrespective of gender and social category, have access to education. An education that enables them to acquire skills, knowledge, values and attitudes necessary to become responsible and active citizens of India". Enhancing employability of the labour force requires focus on both skill development and an economic structure that could ensure that the growth process become more employment intensive.

According to the national skill development policy 2009, the current capacity of the country to conduct skill development programmes is about 3.1 million. The target is to cover 500 million cumulatively by 2022. The policy recognizes that 93 per cent of the country's workforce is in the unorganized sector, but contributes only 60 per cent of GDP. Strengthening the skill base in this segment will contribute to improving productivity, working conditions and living standards.

When we talk of living standards what is of immediate relevance is shelter. The right to shelter is as important as the right to education and employment. Now, since the past decade or so there has been a tremendous demand for housing as the economy flourished and income levels increased significantly. The banks entering the housing finance market in a big way provided a major fillip to this sector. But when we talk of shelter to all we mean housing units which will be within the reach of the common man. To bring down the unit cost of housing to that level would require a great deal of technological and financial innovation.

To deal with the challenge of gainfully absorbing the expected large number of new entrants to the job market, the Government has set a target of raising the share of manufacturing in GDP from the current level of about 16 per cent to 25 per cent by 2025.

But there are huge challenges here. Power will be the major challenge. The International Energy Agency estimates suggest that the shares of India and China in the world fossil fuel demand by 2030 will be 16 per cent and 38 per cent, respectively.

Alternative clean energy and energy security will be critical for India in the years to come, and this would require innovative ideas from the youth and timely investment by the private sector, with necessary support and an enabling policy environment from the Government.

Hon'ble President of India had emphasized while addressing the students of IIT, Kanpur in 2010 that "...The next ten years, declared as the Decade of Innovation, can be a fruitful decade in India. Qualified and talented individuals of our nation have to find innovative solutions to our myriad challenges, keeping in mind our specific conditions".

The voice of the youth and the private business enterprises would need to ensure food security along with energy security. A country with 1.2 billion population can ill afford to depend on the outside world for meeting its needs for energy or basic food. Adverse shocks from these two sources have, as you all know, often led to high inflation, which in turn becomes a risk to sustainable high growth. Higher agricultural productivity and adequate investment to increase the supply of protein rich food items would require a new revolution, driven by new technology and additional investment. As the average income of the young population increases with high growth, demand for items like milk, meat, eggs, fruits, vegetables and pulses will increase, and without necessary supply augmentation, containing inflation will become a difficult challenge.

When I say we must raise our productivity I do not compare ourselves with America or other countries. I am talking about inter-regional comparisons within our own country. We say one reason for inflation going up is people are drinking more milk. How can milk prices come down if do not produce more milk? Why our success in Anand experiment cannot be replicated in other parts of the country? Only when productivity goes up and cost comes down, can inflation be curbed. We need to innovate to emulate at least our own Indian benchmarks and best practices to meet the productivity challenge.

When I stress on the importance of innovative ideas, I must also caution that destructive innovations that led to the global financial crisis are not in the interest of anyone. The field of finance and banking often attracts the best from among the youth. Any misuse of the financial system – caused by the actions of a few smart educated individuals – could impact the life of a billion plus population. I need not emphasize the importance of ethics and value systems to this audience. India avoided a financial crisis at home in the midst of a severe global contagion. It is our collective responsibility to raise this ethical awareness. Trusted newspapers such as The Hindu can take the lead here.

One cannot look to the government to solve every problem. Similarly banks cannot provide solutions to all your needs. It is the responsibility of everybody to build the future of tomorrow. That includes civil society such as the Save Nilgiris Campaign which is doing good work in the Nilgiris. Government and banks can at best facilitate the process of economic development.

Let me take the example of quality education and housing mentioned earlier. Recent estimates suggest that for every one percent increase in GDP, demand for education loan increases by 3 per cent, and demand for housing loans increases by 5 per cent. Given the demography, as income increases, more and more students would aspire to get quality education, as a means to a better future. On the other hand, the costs of private quality education seem to be increasing significantly in recent years. After education, once they get gainful employment, decent housing will be the next aspiration. While banks will have to meet the aspirations of the youth by ensuring access to credit at competitive price, to get quality education and shelter, the private sector would have to recognize that artificially created inflation driven by unreasonable profit motives in these two critical segments would be a constraint to our growth and development ambitions.

This leads to me to another critical challenge to our future growth – *i.e.* inclusive growth. High growth that coexists with rising inequality will become unsustainable at some point. As inclusive growth is not possible without financial inclusion, the RBI's vision is that everyone in the country should first have access to financial products and services, which is being achieved in phased manner. The rationale behind this is that access to finance, along with fair and transparent products/services, is a source of empowerment and allows people to participate more effectively in the economic and social process. Our dream of inclusive growth cannot be realized unless we properly educate and make employable the future generation of youth and create millions of micro-entrepreneurs across the country.