K C Chakrabarty: Indian economy – imperatives for second generation reforms

Address by Dr K C Chakrabarty, Deputy Governor of the Reserve Bank of India, at the inaugural session of the State level seminar, organized by the Department of Economics of the Vivekananda Education Society's College of Arts, Science and Commerce, Mumbai, 14 September 2012.

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Dr. Suresh Kotak, Chairman, Kotak and Co. Ltd.; Dr. J. Phadnis, Principal of the VES College of Arts, Science and Commerce; Shri B.L. Boolani, Trustee In-charge; Dr. Suniti Nagpurkar, Head of the Economics Department and Convener of the Seminar, Mrs. Dipta Dasgupta, my old friend from the Banaras Hindu University; faculty members and students participating in the Seminar, Ladies and Gentlemen. It is, indeed, a matter of great pleasure and privilege for me that I have been called upon to address today's Seminar, which indeed is topical, given the changing contours of the financial regulatory architecture amidst uncertain global financial market environment. The global banking and financial system is currently undergoing structural transformation with standard setting institutions and national authorities framing new regulatory paradigms to address the weaknesses of the global financial system that surfaced during the crisis. Against this backdrop, I am delighted that the Vivekananda Education Society is conducting this State level Seminar on this subject.

The Vivekananda Education Society, which started its educational activities in 1962, today imparts education to more than 18000 students ranging from primary school to advanced learning in diverse areas such as management, law, engineering, science, etc. With a mission of "Pursuit of Excellence in Higher Education", the society has sought to impart quality education and help in character building in students. I am told that the society and this college in particular, were set up to cater to the needs of the socially and economically weaker sections of the population, in line with the recognition that education provides opportunities for improvement in quality of life of these deprived sections. I congratulate the Society for completion of 50 glorious years and commend its achievements over this period. I hope that it continues its good work in the times to come.

I must admit that interacting with a gathering of teachers and students provides us with an opportunity to get a different perspective on issues from what we normally get while interacting with fellow finance professionals. Besides, interacting with teachers provides a platform to convey our ideas, through you, to a much larger audience consisting of young minds who will define the path that the country and the financial sector will take in the years to come. It is, hence, a great pleasure for me to be here today.

Swami Vivekananda – a great reformer himself

On the eve of the Golden Jubilee celebrations of the Vivekananda Education Society, it is apt to recall Swami Vivekananda, from whom the College derives its name and inspiration. Swami Vivekananda was a great thinker and reformer of India who envisioned a new educational model for the society. His valuable thoughts on education are relevant and viable even today. According to him, "education is the manifestation of the perfection already in man". He said "mere book-learning won't do. We want that education by which character is formed, strength of mind is increased, the intellect is expanded, and by which one can stand on one's own feet". He taught that it is only through education that the upliftment of masses is possible. However, Swami Vivekananda's scheme of education, through which he wanted to build a strong nation that will lead the world towards peace and harmony, is still a far cry. It is high time that we give serious thought to his philosophy of education and remember his call to every-body – "Arise, awake, and stop not till the goal is reached." I hope the society pursues this vision of Swami Vivekananda.

Swamiji's most unique contribution to the creation of new India was to open the minds of Indians to their duty to the downtrodden masses. He was the first religious leader in India to understand and openly declare that the real cause of India's deep rooted problems was the neglect of the masses. Long before the ideas of Karl Marx were known in India, Swamiji spoke about the role of the labouring classes in the production of the country's wealth.

Having said this, let me come back to the realm of financial sector reforms in India. As many of you are aware, the Indian financial sector has seen wide ranging reforms during the last two decades. However, these reforms were broader and focused at the macro level with internal reforms at the institutional level yet to take place. Thus, the need of the hour is to go for second generation reforms. Nonetheless, the reforms in the financial sector alone will not bring perpetual prosperity. It is the real sector which needs reforms. The financial sector has to grow and keep pace with the developments in the real sector.

Why financial sector regulation?

On an intuitive basis, the business of finance and banking is different from other businesses. This is on account of the fact that while other businesses operate with their own funds, banks are highly leveraged institutions that operate with public money and hence, require to be closely regulated and supervised. Besides, unlike other businesses where, due to absence of entry barriers, free market competition can be expected to ensure efficiency and fair treatment of customers, in the banking business, high entry barriers imply that banking operations cannot be carried out without a license. This restricts the free play of competitive forces and hence, makes it all the more imperative to have a sound regulatory framework, particularly for protection of customers. In the business of banking and finance, there is an inherent inequity between the provider of the service and the consumer and this, again, presents the need for a framework of rules and procedures, which we call as regulation.

The health of the financial sector is a matter of public policy concern in view of its critical contribution to economic performance. Financial regulation and supervision assumes importance in ensuring that the financial system operates along sound lines. The primary justification for financial regulation by authorities is to prevent systemic risk, avoid financial crises, protect depositors' interest and reduce asymmetry of information between depositors and banks. As the costs of financial crises are perceived to be very high, the authorities realised that they should be avoided at all costs. As a result, banks came to be regulated everywhere. Besides, financial regulation attempts to enhance the efficiency of the financial system and to achieve a broad range of social objectives. Going by the experience in several countries, effective regulation is in the interests of all concerned, though it cannot be based on a "one-size-fits-all" approach. However, it is important to bear in mind that while financial institutions do benefit from an appropriate regulatory regime, there is not much evidence that the existence of a regulatory jurisdiction makes institutions stronger and less prone to shocks. There is neither a unique theoretical model, nor just one practical approach to the regulation and supervision of a financial system. The existence of different types of regulatory models of the financial system makes the ideal choice a difficult exercise.

The regulation and supervision of the financial system in India is carried out by different regulatory authorities. The Reserve Bank regulates and supervises the major part of the financial system. In the past five decades, the Indian banking system has traversed through a difficult path endeavoring to balance several competing and conflicting demands on it from large, medium, small and tiny borrowers in both the organised and unorganised sectors. The banking system's activities were initially tightly regulated and their freedom was restricted. It also confronted several domestic stresses and external shocks. However, the regulations have changed over time to ensure that the banking system steps out of the restrictive operational environment and functions in an atmosphere that provides the freedom to innovate.

In recent years, innovations in instruments and processes, advances in technology and the increasing volumes of capital intermediated by the financial system have necessitated a proactive strengthening of the regulatory and supervisory framework. Emergence of several players with diversified and significant presence in the financial sector makes it imperative for supervision and regulation to be spread across various segments of the financial system. In recent years, there has been a shift in emphasis from microregulation to macro-management, supported by a tightening of prudential norms and improvements in the functioning of the financial system.

Since the global crisis, there has been a decisive shift in trend towards assigning increased responsibility to the central banks for both “systemic oversight” and “macro-prudential regulation”. This greater responsibility is driven by the capability of the central banks among regulators and public institutions to perform the intended task. Central banks have robust frameworks for macroeconomic analysis, and in India, the Reserve Bank has the responsibility for micro-prudential supervision of banks and non-banking financial companies. As a result, while macroeconomic analysis has helped in strengthening the microprudential supervision, supervisory information aggregated for the financial system as a whole has also helped in conducting more appropriate macroeconomic policies.

The Reserve Bank has been deeply involved in the development of markets, and it monitors and analyses the impact of market trends on the economy and financial institutions. Another important reason why central banks have to be the systemic risk regulator is because of their mandate of Lender of Last Resort (LOLR). Going forward, given the complex nature of the challenge, significant strengthening of the capacity for systemic risk assessment and macro-prudential regulation would be critical for the Reserve Bank.

Macroeconomic and financial sector reforms

In response to the macroeconomic crisis, a programme of stabilisation and structural adjustment was initiated in July 1991, with wide ranging reform measures encompassing the areas of trade, exchange rate management, industry, public finance and the financial sector. Fiscal correction, exchange rate adjustment, monetary targets and inflation controls constituted the immediate measures for macroeconomic stability. These measures were supported by structural reforms in the form of industrial deregulation, liberalisation of foreign direct investment, trade liberalisation, overhauling of public enterprises and financial sector reforms. Apart from aiming at restoring the economic stability on both domestic and external fronts, the economic reform programme strived towards achieving a higher growth trajectory through increased levels of investment and improvements in productivity, efficiency and competitiveness. Structural reforms aimed at reorientation of the economy from a centrally directed command and control economy to a market oriented one to foster greater efficiency and growth. This was done by introducing greater competition in the economy through progressive internal deregulation accompanied by external competition promoted by foreign direct investment and trade liberalisation.

The reform measures had sectoral dimensions as well. Beginning with the industrial policy of 1991, reforms in the industrial sector were undertaken with a view to remove distortions in the resource allocation and improve competitiveness of Indian industry. The reform measures included removal of industrial licensing, reduction in the number of industries reserved for the public sector, abolition of restrictions on investment and expansion under the Monopolies and Restrictive Trade Practices (MRTP)Act, 1969, automatic approval of foreign investment, elimination of quantitative import restrictions on intermediate and capital goods and steady reduction in protective customs tariffs. These measures created a favourable environment for industry to upgrade its technology and build-up capacity in order to cater to growing domestic and external demand. A series of policy initiatives were undertaken in agricultural sector as well. These included, *inter alia,* replacement of quantitative controls by tariffs, partial decontrol of fertilizer prices, removal of bottlenecks in agricultural marketing, relaxation of restrictions of the Essential Commodities Act, 1955, replacement of the Revamped Public Distribution System (RPDS) with Targeted Public Distribution System (TPDS), and establishment of Rural Infrastructure Development Fund (RIDF). Moreover, price reforms improved terms of trade for agriculture. Also, exchange rate and international trade reforms improved the incentive structure facing agriculture.

Several initiatives were undertaken for the development and reform of financial markets, particularly since the 1990s. The reforms in various segments of financial markets such as money, the government securities and the foreign exchange markets were introduced in a calibrated, sequenced and careful manner, in step with those in other markets in the real economy. The sequencing has also been informed by the need to develop market infrastructure, technology and capabilities of market participants and financial institutions in a consistent manner. In India, the initiation of the structural reforms in the early 1990s encompassed a process of phased and coordinated deregulation and liberalisation of financial markets. Financial markets in India, in the period before the early 1990s, were marked by administered interest rates, quantitative ceilings, statutory pre-emptions, captive market for government securities, excessive reliance on central bank financing, pegged exchange rate, and current and capital account restrictions. As a result of various reforms, the financial markets have transited to a regime characterised by market-determined interest and exchange rates, price-based instruments of monetary policy, current account convertibility, phased capital account liberalisation and an auction-based system in the government securities market. Enhancing efficiency, while at the same time avoiding instability in the system, has been the challenge for the regulators in India. This approach to development and regulation of financial markets has imparted it greater resilience. India's reform programme has had a definite positive and significant impact on the economy as compared with the past.

Who are the stakeholders?

In the whole process of reforms, the key stakeholders are the customers themselves. The regulators have a critical role in ensuring fair treatment to customers and it cannot be left to the market forces alone. The key to a prompt, effective and courteous customer service emanates from having the right attitude. A radical transformation of attitude right from Top Management to ground level employees is the first step towards improving customer service. Communication is at the root of effective customer care in a service industry, especially like banking, where the documents, terms and conditions, practices and precedents are all heavily loaded against the customer. In many fields and in different countries, regulators determine the price. But, the financial sector regulator in India does not do so. Therefore, whatever charges are levied, it is expected that they are reasonable and that the pricing is fair, transparent and non-discriminatory. Globally, regulators are expected to usher in much stricter regulations in the area of fair treatment to customers. Banks need to price their products and services fairly and competitively and ensure higher transparency in their products and pricing. Lack of transparency in designing and pricing of products and services and selling them to inappropriate customers could expose banks to litigation and reputational risks, besides making them liable for supervisory action. There should be no unreasonable post sale barriers if the customers wish to change product or bank. Customer education is also critical in providing appropriate and need based products and services and the Indian Banks' Association may have a critical role to play in this regard. The banking business would, thus, have to turn customer centric in all its true dimensions.

Financial sector reforms – what next?

The Indian approach to financial sector reforms, so far, has been driven by the predominant objective of enhancing the role of finance in promoting growth and economic development, while preserving financial stability, which is equally critical for sustained economic progress. While balancing the goals of efficiency and stability in introducing reforms, the Reserve Bank has moved towards deregulation of interest rates, promoted development of markets, and strengthened the legal infrastructure to facilitate better enforcement of financial contracts. Going forward, three areas will continue to be important in policy debates, *i.e.,* development of long-term corporate bond markets, derivative markets to facilitate better price discovery and risk transfers, and more competition by allowing greater foreign participation.

The regulatory and supervisory framework of the financial system across the world is undergoing a paradigm shift following the problems experienced during the global financial crisis. In this regard, multilateral and standard setting bodies like the G-20, IMF, BIS and FSB have been in the forefront to design an advanced regulatory framework to prevent the recurrence of such crisis. Addressing the regulatory gaps based on the lessons from the global financial crisis in advanced economies will be a major challenge for regulators all around the world. Much of the challenges in the domain of financial stability regulation would arise from complexities surrounding the assessment of systemic risk, interconnectedness, common exposures, risk concentrations in complex innovative products and use of models to manage and price risks which, at times, mask information.

While India's financial sector remained resilient in the face of global shocks, there are a number of areas where the reforms would be needed to promote stability and generate growth impulses for the real economy. In the wake of turbulent global financial environment, banks and financial entities have to grapple with growing complexities and risks associated with their businesses. Against this backdrop, the policy initiatives such as adoption of tighter capital and liquidity standards, improved risk management practices and sound compensation practices are required to place the Indian banking system on a strong footing and enhance the banking sector's ability to absorb shocks arising from any financial and economic stress and encourage prudent risk taking.

Moreover, in India, while broader institutional reforms have taken place at the macro level, the internal reforms among banks and financial institutions are yet to take place. Thus, there is a need to go for second generation reforms, particularly focusing on bringing down the cost of banking services, strengthening the credit delivery mechanism, improving customer service, reforming the human resources management systems and enhancing the financial outreach to hitherto unbanked areas.

Second generation reforms

Let me talk about some of the elements of these second generation reforms.

(i) Adopting improved risk management practices

One fundamental principal of finance that I would like to emphasize is the direct relationship between risk and return. Any investment that offers greater returns, invariably involves more risk. Similarly, if you avoid taking risk, then the returns could even be negative. Banks, for instance, are in the business of taking risks and hence, cannot be expected to shun risk in its entirety. Four basic requirements that banks and professionals in the field need to develop is to:

- Understand Risk
- Define Risk
- Measure Risk
- Manage Risk

My advice to all students entering the finance field would be that never take a risk where you cannot meet the above four requirements.

Globally, there is an increasing move towards more advanced approaches to risk management. Banks in India have made progress in moving towards the advanced risk management approaches. Banks, however, need to traverse a long distance in this regard. As capital always comes at a cost, banks need to have in place a fair and differentiated risk pricing of products and services. This involves costing, quantitative assessment of revenue streams from each product and service and an efficient Transfer Pricing Mechanism, which would determine capital allocation. Each business unit in the enterprise would have to aim at being a profit centre within the overall risk–return framework. In essence, it would mean accountability for profit, tempered by the discipline of risk–return within a deeply embedded culture of good governance. Our past experience has been of poor savers subsidising the rich borrowers. Also, there are incidences of rampant mis-pricing of risks. From a business perspective, pricing of assets should be non-discriminatory and in line with risk rating of the customer. A lower rated customer should not get a better price than a higher rated customer. Once these basic issues are addressed, other issues such as migration to advanced approaches, etc. would gain importance.

While all Indian banks have adopted the standardised approaches under the Basel II framework in 2009, the pace of migration to the advanced approaches has, naturally, been very slow. Though the Reserve Bank has set an indicative time schedule for implementation of the Advanced Approaches, banks' response has been less than encouraging so far. Migration to the Advanced Approaches is important for larger banks as it involves adoption of more sophisticated risk management systems. Moreover, there are reputational issues also in large banks continuing with standardised approaches. Apart from these fundamental issues, much of this sluggishness could be attributed to issues relating to development of human resource skills, technology upgradation, branch interconnectivity, availability and management of historical data, robustness of risk management systems, *etc*. within the banks. Even within the Reserve Bank, the supervisors would have to make rapid strides to be able to appreciate the nuances associated with the quantitative techniques and models.

The objective of the Basle III reform package is to improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source, thus reducing the risk of spillover from the financial sector to the real economy. An assessment of Indian banks' capital requirements under Basel III has revealed that, notwithstanding some issues with a few individual banks, the system as a whole, is very well capitalised and the transition to the revised capital norms of overall capital adequacy, Tier I component or equity component would be smooth. The implementation period of Basel III capital requirements, including capital conservation buffer and regulatory deductions, will begin from January 1, 2013 and will be fully implemented by March 31, 2018, before the timeline (January 1, 2019) indicated in Basel III rules.

(ii) Reforming human resources management

There is an imperative need to improve the productivity and efficiency of human resources. An organisation can only be as good as its people. They are the force behind innovation, business process re-engineering and making the difference between success and failure. A committed and highly motivated work force can make the difference in winning and retaining customers as banking is a people oriented business. Banks have to be knowledge organisations, able to attract and retain talent. HR policies should look at right size, right fit and career growth with market related compensation. Increasingly, there is going to be intense competition for the right kind of talent as they are likely to be in short supply. The demand for efficient manpower will not only stem from domestic institutions but also from foreign institutions/ countries; and not just from the banking industry but from other financial/non-financial sectors. The challenge before Indian banks is, therefore, to revitalise themselves by hiring the right talent, investing in training and bringing about a vibrant transformation in their DNA.

(iii) Technology to be more customer focused

Most banks are already on Core Banking Systems (CBS) which covers banking operations pertaining to deposits, withdrawals, credit delivery, back-office operations, *etc.* Banks need to look beyond Core Banking to harness the benefits of technology. CBS could provide inputs for developing customised products based on customer database. It would help in planning product delivery and service at selected/ multiple delivery points, better Customer Relationship Management and building lasting customer relationships which will translate into higher revenues. Technology needs to be more customer focused than employee or vendor focused. In case of glitches, the rectification must be swift to instill faith and confidence in the system. It is only the more agile and innovative players who will stay ahead in the game. Along with IT solutions arise allied issues such as IT security, governance and audits. Gaps in IT security could make banks vulnerable to data piracy, fraud and operational risk leading to reputation risk and erosion of customer confidence.

(iv) Focusing on MIS and information literacy

MIS is an inseparable part of bank's decision making process. The integrity and timeliness of data is critical in formulating the bank's capital planning, business strategies, reviewing achievements *vis-a-vis* targets, formulating course correction exercises where required, feeding data into stress tests and importantly, taking action on the outcomes. This brings us to technology support for decision making. Banks have made huge investments in technology, which should be translated into better MIS through decision support systems and yield returns on investment by providing economical, affordable and customised customer centric banking solutions. The use of technology should not be seen as an end in itself but as a means to an end.

(v) Business strategy and vision

The role of banks' Boards would become increasingly crucial in the next decade in view of the looming competition. The Board would need to have a clear vision for the bank, a strategy to achieve its objectives, both medium and long-term, and a well laid out long-term plan. Banks would need to look beyond their existing customer base and large corporates and reach out to rope in the vast number of small, retail and SME clients which are presently deprived of bank credit. Alongside extending the reach of their banking services, there would be a need to improve the products offered to customers and the quality of services. They need to have proper business model and delivery model.

(vi) Reaching to the unbanked / under-banked areas

In India, growth with equity has been the central objective right from the inception of the planning process. The objective of financial inclusion is to provide financial services at affordable cost to those who are excluded from the formal financial system. This is vital for sustaining long term equitable development, since a large proportion of the households/areas do not have access to basic banking facilities, notwithstanding the existence of vast institutional framework in the country. An important challenge is to channelise more savings to the financial system, particularly in rural areas and from the urban informal sector. This would need further penetration of the banking system. The Reserve Bank's emphasis on financial inclusion is important in attaining this objective over time. There is also enormous potential for extending finance in semi-urban and rural areas for productive activities, which may require strengthening the banking correspondent relationship, simultaneously enhancing the risk assessment and risk management capacities in order to maintain credit quality and sustain the credit growth in these sectors. Besides benefiting the unbanked masses, this will also ensure viability and scalability of banks' financial inclusion initiatives.

(vii) Bringing down the cost of banking services

Further reduction in the cost of banking services may require greater competition among product lines, improved delivery mechanisms and increasing use of information technology. The costs of banking transactions need to be dramatically reduced as has happened in many other fields such as telecom, after the advent of technology. However, it is observed that, in banking, the transaction costs continue to be high, particularly in agriculture sector, which include costs incurred in appraisal of borrowers, processing, documentation and disbursement charges, loan monitoring/supervision and collection. It is essential to bring down such transaction costs to make available credit at affordable price to the farmers.

Balancing the real and financial sector reforms

Financial sector reforms alone will not bring continued prosperity. In the recent years, we see, growing evidence on growth deceleration in the Indian economy. For sustaining the high growth path, improving the investment climate and enhancing the absorptive capacity by bringing in the real sector reforms would be critical. The fact that a well-developed financial sector is necessary to act as the intermediary between entrepreneurs/ investors and savers can hardly be overstated. An efficient financial sector reduces the cost and risk of producing and trading goods and services and, thus, makes an important contribution to raising standards of living. The recent crisis, however, showed that the financial sector had apparently taken a quasi-autonomous existence without close connection with the financing requirements of the real economy. The financial industry, indeed, grew oversized in the preceding years, reflected in rapid credit creation, asset price bubbles and high levels of indebtedness, particularly in advanced financial systems. The disproportionate growth in the global financial sector was largely due to the aggressive search for yield, engendered by the easy liquidity in the global system that triggered a wave of financial innovation. Complex financial products were created by structuring and hedging, originating and distributing, all under the belief that real value could be created by sheer financial engineering. There were hardly any signs of growing capital formation due to the growing and increasingly complex financial sector.

The financial sector grew more rapidly than other goods and services. In a way, that made growth of finance an end in itself and not a means to meet human needs such as food, fuel, health and education. Given that the busting of the oversized financial sector has a devastating impact on the real sector, it becomes important to (i) examine the optimal size of the financial sector relative to growth and development needs and (ii) make financial sector innovations more meaningful to cater to the needs of the real sector.

For sustaining the high growth path, it is imperative that we bring in reforms in the agriculture, industry, infrastructure and services sectors. I would like touch upon some of the elements of these reforms.

Improving agricultural governance and productivity

In order to step up agriculture growth, a judicious use of technology is required along with institutional reforms, including those relating to land, incentives for supply response and better input use. Given the dependence of a vast majority of workforce on agriculture, enhancing the agricultural output, driven by higher yield and diversification of crops, assumes importance. Higher investment, backed by sustained research and extension activities, could be critical for augmenting yield. The policy focus, so far, has been on using higher MSP to generate supply response and public investment on expanding the irrigation potential. However, there is a need for improving the market structure for agricultural commodities, ensuring competitive pricing, enhancing warehouse facilities and improving rural roads for enhancing better connectivity with urban markets. Better water management, with an emphasis on water harvesting, would be important for enhancing the farm productivity and output.

Improving the performance of manufacturing sector

The manufacturing sector's performance in a competitive environment and in the face of risks of rising protectionism could encounter several challenges. Despite the advantages of a large domestic market, abundant availability of skilled labour force, and the proximity to the fast growing Asian markets, productivity growth needs to catch up with the Asian economies, including China. This requires greater emphasis on quality, better adoption of technology, more flexible labour laws, significantly improved infrastructure and a policy environment supportive of the SMEs sector. The industry-education linkages must be strengthened vigorously. Persistent problems like frequent disruptions in the availability of power and lack of stable demand also affect the performance of the manufacturing sector.

Harnessing the potential of services sector

Notwithstanding the high growth and resilience of the services sector in the recent past, the sector faces multiple challenges for sustained growth over the years. A number of services, where India enjoys comparative advantage, experience lack of clear policy thrust. For instance, despite the high quality of healthcare services, it attracts a number of regulations. Similarly, in education, multiple regulation points and lack of credible accreditation systems hamper the growth potential. Given the medium to long-term contribution of investments on education and health to growth and productivity, availability of these services at affordable cost, while enhancing their global competitiveness, must form part of the priority in India's development process. A number of services in India are either predominantly associated with the Government or not liberalised enough to ensure growth through organised private initiatives. Services like professional, legal, postal, accountancy and insurance need further liberalisation to harness their potential.

Facilitating infrastructure finance

As per the assessment of the Planning Commission, during the Twelfth Plan (2012–17) India may need infrastructure investments of over US$ 1trillion. This poses a mammoth financing task. The infrastructure gap in India, both in relation to other major countries and its own growing demand, has been a key factor affecting the overall productivity of investments. The requirement of high initial capital outlay, that took over longer terms, necessitates measures to address the financing constraint to capacity expansion in infrastructure. The financing issue relates not only to possible resource gap, but also to ensure commercially viable funding that remains so over business cycles. Infrastructure investment during the Twelfth Plan will need to be funded by both, public and private sectors. Despite increasing participation of the private sector in bridging the infrastructure gap, public investment still has to play a significant role. Fiscal consolidation and reorientation of expenditure towards capital expenditure is required to meet the target. The banking system, despite the risk of asset-liability mismatch while lending for long-term infrastructure projects, has seen high growth in credit to this sector in recent years.

To sum up

The first round of financial sector reforms resulted in strengthening of the financial system and making it more vibrant and resilient. However, over time, the pace of reforms and growth has slowed down and the need for second generation of reforms is strongly felt. These reforms would have to focus on individuals and corporates and work towards improvement in productivity and efficiency of the economy as a whole.

Financial sector reforms, in isolation, will not have a significant impact unless there is improvement in the absorption capacity of the economy. Real sector reforms should precede financial sector reforms for bringing in inclusive and sustainable development of the country. Even in the financial sector, there is an imperative need for internal institutional reforms, particularly focusing on improving the risk management practices, reducing the cost of transactions, both borrowing and lending, and improving the overall customer service. I hope all concerned stakeholders work towards implementation of these second generation reforms, which is essential for moving the economy back to the high growth trajectory.

I would, once again, like to congratulate the Vivekananda Education Society for completion of 50 glorious years and hope that the Society continues its efforts to produce students who are fully equipped to shoulder the responsibility of taking the nation forward in the coming years. I would also urge the management, faculty and students to rededicate themselves towards further broadening the activities and reach of the Society so that it provides an avenue for the deprived segments to attain social and economic prosperity through education. This would be in line with the message that Swami Vivekananda sought to spread, all through his life, through his work and writings.

I wish the deliberations of the Seminar all success. Thank you.