

RBI's Proposed Measures to Strengthen India's Banking System

A comprehensive overview of regulatory reforms to enhance financial stability and risk management in Indian banking



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Context & Need for Reform



Regulatory Evolution

The Reserve Bank of India has undertaken a comprehensive review of banking regulations to align with global best practices and address emerging risks in the financial system.

These measures aim to strengthen the resilience of Indian banks, enhance depositor protection, and ensure long-term financial stability in an evolving economic landscape.



Financial Stability

Strengthening systemic resilience

Risk Management

Proactive identification and mitigation

Global Alignment

Harmonizing with international standards

Measure 1: Risk-Based Deposit Insurance Premiums



Transitioning to Risk-Sensitive Pricing

The RBI proposes moving from a flat-rate deposit insurance premium system to a **risk-based approach** that aligns premium costs with individual bank risk profiles. This methodology ensures banks with higher risk exposures contribute proportionately more to the deposit insurance fund.

Current System

Uniform premium rate applied equally to all banks regardless of their risk profile or financial health indicators

Proposed Model

Differentiated premiums based on capital adequacy, asset quality, management quality, earnings, and liquidity metrics

Expected Benefits

Incentivizes prudent risk management practices and creates a more equitable premium distribution framework

Bank Deposit
Insurance
Protection



Measure 2: Expected Credit Loss Framework

Forward-Looking Provisioning Approach

The RBI is introducing an **Expected Credit Loss (ECL)** framework to replace the existing incurred loss model. This represents a fundamental shift in how banks recognize and provision for credit losses.

Under ECL, banks must anticipate potential losses based on forward-looking information rather than waiting for actual default events, enhancing early risk detection and financial resilience.

Key Implementation Aspects

- Incorporation of macroeconomic forecasts and historical data
- Stage –based classification of financial assets
- Enhanced disclosure and transparency requirements
- Alignment with IFRS 9 international standards



Measure 3: Revised Basel III Capital Norms

Strengthening Capital Adequacy Standards

The Reserve Bank proposes comprehensive revisions to Basel III capital requirements, introducing more stringent norms for **credit risk, operational risk, and market risk** calculations. These enhanced standards ensure banks maintain robust capital buffers to absorb potential losses.



Credit Risk

Enhanced risk weighting methodologies for loan portfolios and counterparty exposures



Operational Risk

Standardized measurement approach for operational failures and system risks



Market Risk

Revised frameworks for trading book capital requirements and market volatility



Measure 4: Investment Regulation & Business Overlap Guidelines

Investment Restrictions

Clear guidelines on permissible investments and exposure limits to prevent concentration risks and ensure diversification

Business Overlap Rules

Framework to address conflicts arising from banks' participation in multiple financial service segments

Subsidiary Management

Enhanced oversight requirements for bank subsidiaries and associated entities to maintain regulatory clarity

These guidelines aim to **reduce systemic risk**, prevent regulatory arbitrage, and ensure appropriate boundaries between different financial activities conducted by banking institutions.

Implications for Banks & Financial Stability

Impact on Banking Sector

1

Capital Requirements

Banks will need to maintain higher capital buffers, potentially impacting profitability in the short term

2

Compliance Costs

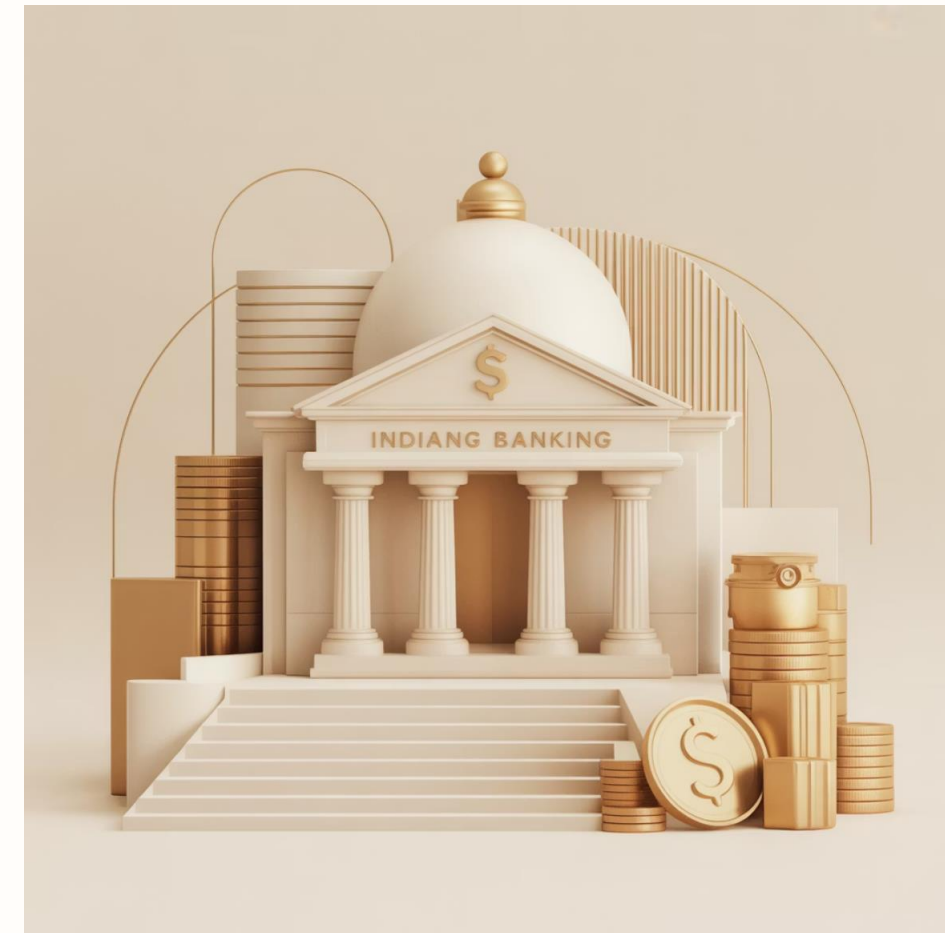
Implementation requires significant investment in systems, processes, and personnel training

3

Risk Management

Enhanced focus on proactive risk identification and mitigation strategies across all business lines

Broader Financial Stability



These measures collectively strengthen the banking system's ability to withstand economic shocks and protect depositor interests.

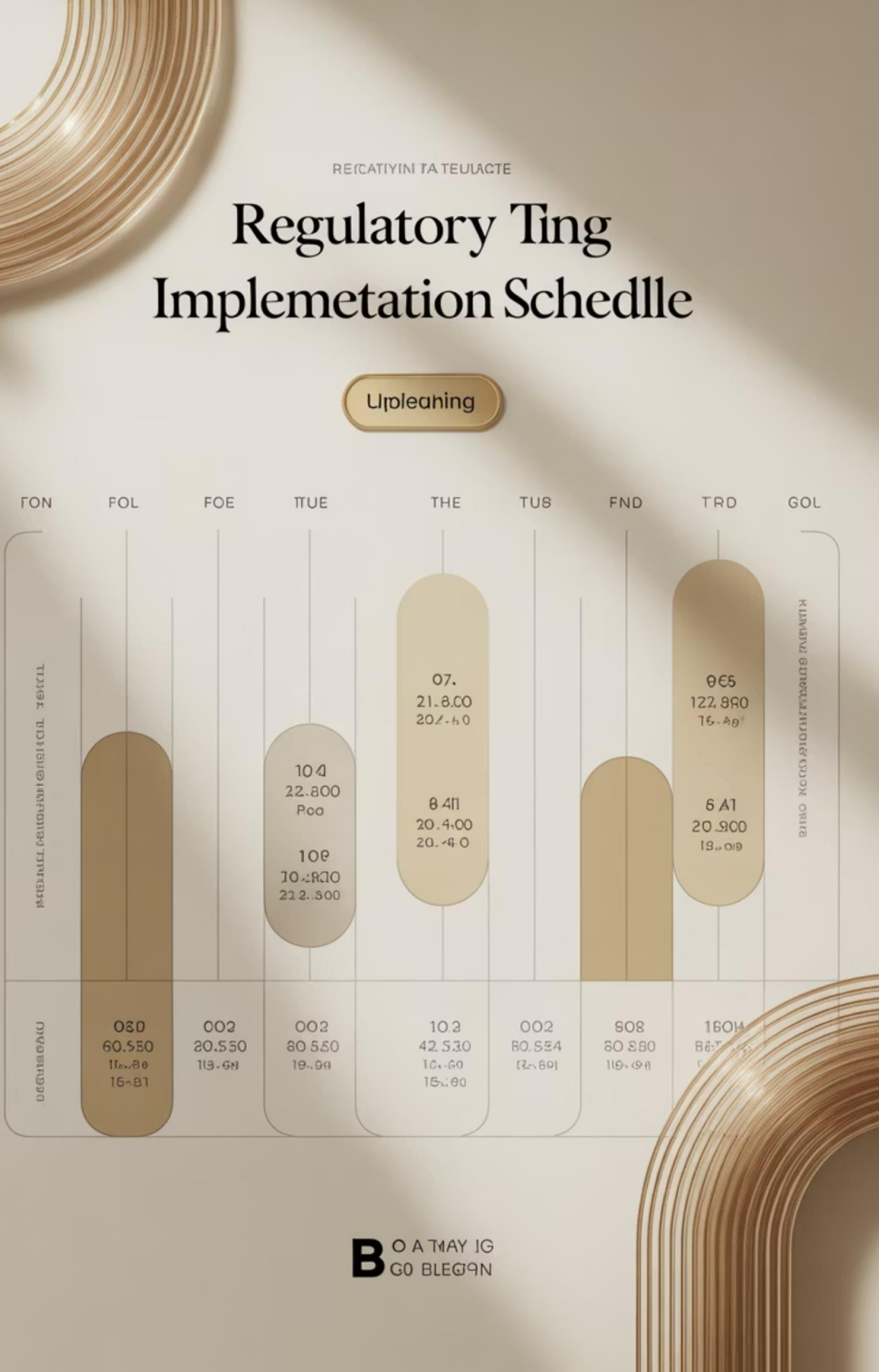
The reforms position India's banking sector for **sustainable long-term growth** while maintaining alignment with international regulatory standards.

Timeline & Next Steps

- 1 Consultation Phase**
Draft guidelines released for stakeholder feedback and industry consultation
- 2 Finalization**
RBI reviews comments and publishes final regulatory framework
- 3 Transition Period**
Banks prepare systems and processes for compliance with new requirements
- 4 Full Implementation**
Complete adoption of all proposed measures across the banking sector



Important: Banks are encouraged to begin preparatory work immediately to ensure smooth transition and timely compliance with the new regulatory framework.



Conclusion



Strengthening India's Banking Future

The RBI's comprehensive regulatory reforms represent a **significant milestone** in fortifying India's banking system. Through risk-based deposit insurance, forward-looking provisioning, enhanced capital norms, and clearer business guidelines, these measures create a more resilient and stable financial ecosystem.

While implementation will require substantial effort and resources from banking institutions, the long-term benefits—**enhanced stability, improved risk management, and stronger depositor protection**—will position India's banking sector for sustained growth and global competitiveness.

Enhanced Resilience

Global Standards

Depositor Protection

Sustainable Growth