

RBI's Financial Stability Report, January 2021

January 13, 2021

In news

The Reserve bank of India releases the 22nd issue of the Financial Stability Report (FSR)

About the Financial Stability Report (FSR)

The report reflects the collective assessment of the Sub-Committee of the Financial Stability and Development Council (FSDC) on risks to financial stability, and the resilience of the financial system in the context of contemporaneous issues relating to development and regulation of the financial sector.

The release of FSR was rescheduled to incorporate the first advance estimates of national income for 2020-21 that were released by the National Statistical Office on January 7, 2021

Key highlights of the report

- **Policy actions during Covid-19:** The report states that in the initial phase of the COVID-19 pandemic, policy actions were geared towards restoring normal functioning and mitigating stress; the focus is now being oriented towards supporting the recovery and preserving the solvency of businesses and households.
- Positive news on vaccine development has underpinned optimism on the outlook, though it is marred by a second wave of the virus including more virulent strains.
- **Policy measures:** As per the report, **policy measures by the regulators and the government have ensured the smooth functioning of domestic markets and financial institutions;** managing market volatility amidst rising

spillovers has become challenging especially when the movements in certain segments of the financial markets are not in sync with developments in the real sector.

- **Bank credit growth:** According to FSR, Bank credit growth has remained subdued, with the moderation being broad-based across bank groups.
- **Performance parameters of banks:** FSR mentions that performance parameters of banks have improved significantly, aided by regulatory dispensations extended in response to the COVID-19 pandemic.
- **CRAR:** The report mentions that the capital to risk-weighted assets ratio (CRAR) of Scheduled Commercial Banks (SCBs) improved to 15.8 per cent in September 2020 from 14.7 per cent in March 2020
- **GNPA:** According to the report, SCBs gross non-performing asset (GNPA) ratio declined to 7.5 per cent from 8.4 per cent, and the provision coverage ratio (PCR) improved to 72.4 per cent from 66.2 per cent over this period.
- **GNPA may increase as per advance estimates of gross domestic product (GDP):**
 - As per the report, macro stress tests incorporating the first advance estimates of gross domestic product (GDP) for 2020-21 released on January 7, 2021 indicate that the GNPA ratio of all SCBs may increase from 7.5 per cent in September 2020 to 13.5 per cent by September 2021 under the baseline scenario
 - The ratio may escalate to 14.8 per cent under a severe stress scenario.
 - This highlights the need for proactive building up of adequate capital to withstand possible asset quality deterioration.
- **Bilateral exposures:** Network analysis reveals that total bilateral exposures among entities in the financial system increased marginally during the quarter-ended September 2020.
- **Declined risk to banking system:** With the inter-bank

market continuing to shrink and with better capitalisation of banks, the contagion risk to the banking system under various scenarios declined as compared to March 2020.

About the Financial Stability and Development Council (FSDC)

- It is a super regulatory body constituted by the government of India which deals with macro prudential and financial regularities in the entire financial sector of India.
- FSDC has replaced the High Level Coordination Committee on Financial Markets (HLCCFM), which was facilitating regulatory coordination, though informally, prior to the setting up of FSDC.
- It is not a statutory body and only a recommendatory body
- Chairperson: The Union Finance Minister of India
- Members: Heads of the financial sector regulatory authorities (i.e., RBI, SEBI, IRDA, and PFRDA), Finance Secretary and/or Secretary, Department of Economic Affairs (Union Finance Ministry), Secretary, Department of Financial Services, and Chief Economic Adviser. FSDC can invite experts to its meeting if required.
- The objectives of FSDC would be to deal with issues relating to: Financial stability • Financial sector development • Inter-regulatory coordination • Financial literacy • Financial inclusion • Macro prudential supervision of the economy including the functioning of large financial conglomerates. • Coordinating India's international interface with financial sector bodies such as the Financial Action Task Force (FATF) and Financial Stability Board (FSB).
- FSDC was formed to bring greater coordination among financial market regulators