



Financial Stability Report

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The Reserve Bank of India released its **18th Financial Stability Report (FSR)**. **FSR is a biannual publication.**

- The FSRs are periodic exercise for reviewing the nature, magnitude and implications of risks that may have a bearing on the **macroeconomic environment, financial institutions, markets and infrastructure.**
- These reports also assesses the resilience of the financial sector through **stress tests.** Stress tests are used to gauge how certain unfavorable economic scenarios, such as a deep recession or financial crisis will affect a company, industry or specific portfolio. Stress tests are usually **computer-generated simulation** models that test hypothetical scenarios.
- It reflects the collective assessment of the **Sub-Committee of the Financial Stability and Development Council (FSDC)** on risks to the financial stability of the country, as also the resilience of the financial system.

Findings

- India's financial system **remains stable**, and the **banking sector shows signs of improvement**, even though the global economic environment and the emerging trends in financial sector pose challenges.
 - The reasons for these positive signs include **credit growth of banks** coupled with **improvement in the asset quality of the banks.**
 - Credit growth of scheduled commercial banks (SCBs) has improved between March 2018 and September 2018, driven **largely by private sector banks (PVBs).**
- The global growth outlook for 2018 and 2019 remains steady although the spillover risk to emerging economies because of tightening of financial conditions in Advanced Economies, protectionist trade policies and global geopolitical tension has significantly increased.
- On the domestic front, growth of **gross domestic product (GDP) showed slight**

moderation in Q2:2018-19 while **inflation remains contained**. At present, Inflation is at 2% which falls in the comfortable range of 2% to 6%.

- Slowdown in GDP growth to 7.1%, but there is growth in **Gross Fixed Capital Formation** along with the dip in crude oil prices which are positive for a sustained growth going forward.

Gross Fixed Capital Formation

- Gross fixed capital formation (GFCF) refers to the **net increase in physical assets (investment minus disposals)**. It does not account for the consumption (depreciation) of fixed capital.
- It is a component of **expenditure approach** to calculating Gross Domestic Product (GDP).
- GFCF is **not a measure of total investment**, because only the value of net additions to fixed assets is measured, and all kinds of financial assets, as well as stocks of inventories and other operating costs are excluded.
- Decline in the ratio of gross non-performing assets (GNPA) to advances since September 2015, with both public sector and private sector lenders posting drops in the key indicator of bad loans.
However, State-owned banks continue to have higher levels of bad loans than their private sector peers and are projected to show slower improvements over the second half of the fiscal.
- Recommended solution is **reforms in governance**, while the weaker ones among the public sector banks need to be **supported through recapitalisation**.
- Data on **banking frauds** are also a cause for concern. Close to 95% of the frauds reported in the six months were credit-related, with higher exposure to PSBs.
The graph of **both the frauds as well as the amount** involved has been on the **rise steadily** through the four years till FY18.
- In the wake of the crisis at infra-lender **Infrastructure Leasing & Financial Services (ILFS)** and also a few years after chit fund scams, the RBI pitched for **greater coordination** between **financial sector regulators** to plug any possible gaps which may be exploited by players.

Financial Stability and Development Council (FSDC)

- The Financial Stability and Development Council (FSDC) was set up by the Government as the apex level forum in **December 2010**.
- The objective of FSDC is to strengthen and institutionalize the mechanism for maintaining financial stability, enhancing inter-regulatory coordination and promoting financial sector development.
- The Chairman of the Council is the **Finance Minister** and its members include the heads of all Financial Sector Regulators (RBI, SEBI, PFRDA & IRDA), Finance Secretary

and/or Secretary, Department of Economic Affairs (DEA), Secretary, Department of Financial Services (DFS), and Chief Economic Adviser.

In May, 2018 government reconstituted FSDC to include the Minister of State responsible for the Department of Economic Affairs (DEA), Secretary of Department of Electronics and Information Technology, Chairperson of the Insolvency and Bankruptcy Board of India (IBBI) and the Revenue Secretary.

- **FSDC sub-committee** is headed by the **Governor of RBI**.
- The Council can invite experts to its meeting if required.
- The **Raghuram Rajan committee (2008)** on financial sector reforms first **proposed the creation of FSDC**.