Building inclusive growth in India's financial landscape

Emerging trends in banking, insurance and asset management

June 2024

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Foreword

The theme of 14th Banking & Finance Conference has been rightly chosen by IMC as " Advancing Last Mile Financial Inclusion in Amrit Kaal - Role of Banks and Financial Institutions" In the background of consistent higher real GDP growth of India in the recent past, having become the fifth largest economy in the world and fastest growing economy, it is necessary India should aim becoming a developed economy by 2047 and crossing the third largest Economy at the earliest. Rightly with the opportunity and the potential of Indian Economy to accomplish this objective, India has set for Vikasit Bharat by 2047. At the same time, it should be understood that we have a long way to go and the developed economy presupposes substantial addition to per capita income from the current level and also the reduction of disparities on income levels and reducing substantially inequality in income should be our objective as we have to ensure " Growth with Equity"

United Nations Sustainable Development Goals (SDGs) recognises financial inclusion as a key enabler for achieving Sustainable Development Goals by achieving Universal Financial Access by 2020 has been one of the key developmental agenda of the World Bank. To achieve this ambitious goal, the World Bank group has committed to enable one billion people gain access to a transaction account through targetted interventions.

India being the active member of this group, India has also drawn National Strategy for Financial Inclusion (NSFI) in June 2017 even though in India financial inclusion with access to Bank account, access to credit, access to Insurance, and access to pension started much earlier. This endeavour got strong support and momentum with Pradhan Mantri Jan Dhan Yojana started in 2014 with a big bang approach with spectacular success in a short time which further continued and as on date the beneficiaries more than 50 crores and total balance exceeded Rs 2,03,505 crore. Noteworthy is that 56% JanDhan account holders are women and around 67% Jan Dhan Accounts are in rural and semi-urban areas. It is also gratifying that 33.98 crore Rupay cards issued to PMJDY account holders.

This has been possible with active involvement and participation of banks particularly public sector banks and few active private sector banks and also connecting these accounts with the help of JAM Trinity, Jan Dhan Accounts, Aadhar and Mobile. These accounts also helped in government Direct Benefits Transfer which has expanded to over 300 central schemes and more than 2000 state schemes by April 2023.which has also helped in direct transfer to the benefiaries as well in substantial savings avoiding leakage.

RBI has played a greater role along with the government, has formulated National Strategy for Financial Inclusion 2019-2024 with a view to have a national strategy and action plans with clear targets to provide access to formal financial services in a affordable manner, broadening and deepening financial inclusion and promoting financial literacy and consumer protection.

The push of India to make Digital India with Digital Public Infrastructure and push given for telecommunication density deep in the rural areas has given lot of benefits for financial Inclusion. The newer products launched by National Payment Corporation by UPI products, RTGS, ATMs, massive branch branches in rural areas, unbanned and uncovered areas, introduction of Business Correspondents Channel by RBI, opening of Payment Banks, Small Finance Banks, Financial Literacy and Financial Awareness drive undertaken by govt, RBI and banks and financial institutions etc has resulted in financial Inclusion on a greater scale and as per latest Financial Inclusion Index introduced by RBI, which comprises three broad parameters weights namely Access 35%, Usage 45%, and Quality 20%, rose to 60.1% in March 2023, showing growth in all parameters.

Along with financial inclusion we need to ensure economic inclusion which needs us to empower these customers having lesser income and not much economic activities to engage in, needs to be given access to credit along with savings and make use of various government schemes to put in certain economic activities like micro and small industries, business, trade, rural craft, rural agro related industry, agricultural allied activities, mudra yojana, aspirational district development programme, one district one product, promoting Indian brands abroad by taking up agro and rural related products and the unemployed and under employed youth in rural folk, particularly engagement of women through SHGs etc should enable them to get economically empowered and their income levels will get enhanced . I think that banks and financial institutions have a greater responsibility in this regard and all PMJDY account holders could be potential customers for such credit growth and govt schemes like Credit Guarantee Scheme should help the bank to go forward with these credit growth.

The NBFC sector, Insurance sector and Capital Market Sector like Mutual funds are also playing stupendous role in last mile connectivity and empowerment.

I trust our IMC 14th Banking and finance Event with Eminent speakers with qualitative sessions will enable us to arrive out few useful takeaways for the furthering the objective of Growth with Equity.

Dr. M. Narendra
Chairman, Banking, NBFC and Finance Committee, IMC
& Former CMD, Indian Overseas Bank

Foreword

Insurance sector in India was opened up more than 20 years ago, at the turn of the century, and since then it has made steady progress. Growth rates in India have been much faster than in the developed world.

Yet, India has a long way to traverse. Insurance penetration and insurance density, two key measures of coverage have improved since 2000, but are weak compared to the ratios in developed countries. Many Indians are also under insured, with the insurance cover that they have falling far below their needs, in crucial areas like life and health insurance.

The regulator, IRDAI, has taken several measures, especially in the past two years, to make the sector much more vibrant. In tune with the national aspiration of seeing India as a developed nation by 2047, our 100th year of independence, IRDAI has set a goal of "Insurance for All by 2047". In order that insurance companies can be helped in achieving robust, profitable and sustainable growth, various regulations have been simplified. Product launches becoming easier, by allowing "Use and File" mechanism and payment of commissions to distributors being left to the discretion of the insurance companies, are two examples of major reforms by IRDAI. Government has also opened up the sector to attract the best global practices and technology by allowing 74% FDI.

It is imperative that insurance companies innovate and come up with products and solutions that keep the needs of the customer right at the centre, and as the pivot that will help them achieve success. Insurance, especially in the life sector, is still considered a "push" rather than "pull" product and this needs to rapidly change. A nation's progress depends on the health of its population and ensuring that each and every Indian has access to world class, yet affordable healthcare, is a pressing national need. The government has announced schemes like Ayushman Bharat and insurance companies need to work in tandem to fulfil the national goal.

Reaching out to every Indian with insurance policies that cover their future, needs to be urgently taken up. IRDAI has announced the launch of Bima Vistaar, Bima Vahak and Bima Sugam, three initiatives that are expected to facilitate rapid outreach to the uninsured and underinsured. The regulator has also recently amended the social sector guidelines relating to coverage of the less privileged sections of society. The expectation is that a holistic approach would be taken by the insurance companies to provide cover to each and every eligible individual, village by village, till the whole of India is covered.

Innovation is the key to success. Companies have to become agile to quickly act on the new ecosystem that is much more friendly. In my view, three key aspects will determine success or failure;

a. the ability of companies to leverage technology and offer products and services that add value to customers,
b. effective use of data and analytics by the companies, and
c. investment in their own human resources in the form of proper training as well taking care of the career and life aspirations of the workforce.

It is indeed satisfying that Deloitte is bringing out this knowledge paper on the insurance industry on the occasion of IMC's Annual Finance Conference. I am sure it will benefit all those who are keenly watching the sector and hoping for its success in the days to come.

Arijit Basu
Senior Consultant, AZB Partners, Chairman HDB Financial Services Ltd. & Former MD, SBI

Foreword

Importance of MSMEs in India 2047

India is poised to reach the position of the world's third largest economy very soon and hold on to or improve that standing over the next 25 years. One of the key strengths of the country is its young population and its strong work force which will continue to grow and contribute to its economic strength. But, this "demographic dividend" will be never be realised unless there are employment opportunities for the burgeoning youth. In fact, absence of such opportunities may convert the dividend into a means of social unrest.

It is idle to expect that the government or the large businesses alone will be able to employ our work force. With decline of agriculture as a source of employment, MSMEs have emerged as the key providers of gainful employment. Hence if India has to attain its economic and social goals, a thriving MSME sector is a sine qua non.

Even at present, MSME account for a substantial portion of our GDP both in the manufacturing and services sectors. They also account for a huge part of our exports and it could be expected that the role of MSMEs would only become more and more significant.

One of principal roadblocks to the growth of an MSME is availability of finance. While MSMEs have been part of the priority sector lending obligations for decades, the financial system has not been able to serve them adequately. Inability to understand needs of the sector, rigid lending norms and lack of reliable data relating to the MSME's financial health have hindered the process. Growing digitalisation of the economy, GST implementation, and explosive growth UPI and other digital payments have brought in a much greater formalisation of the sector. It is necessary for the banks and NBFCs to remodel their appraisal methods to account for such huge change in the MSME ecosystem so as to serve them better.

One major hurdle the lenders face is the higher risk associated with MSME exposures. While there have been credit guarantee schemes (such as the CGTMSE) for a long time, their effectiveness has not been optimal. There is a need for creation of more innovative and friendlier credit insurance products to reduce the risk of MSME exposures.

It is heartening to note that the MSME sector has been gradually overcoming its fear of the taxman and becoming more transparent – though this process needs to accelerate significantly. The advent of the newer generation in the managements of MSMEs who are more ambitious and better educated would aid this process. Greater transparency and compliance by MSMEs would enable them to grow faster and in a more sustainable manner and most importantly, enable them to raise external equity capital from venture funds to power their growth.

There is also a need for the government to invest in entrepreneurial skill development for MSMEs. Many MSMEs fail because of lack of knowledge about managing the challenges of growth, which results in over-leveraging and stretched cash flows. Further development of digital marketing ecosystems such as GEMS and ONDC should also help MSMEs in marketing their products and managing their cash flows effectively.

To sum up, the MSMEs can surely play a huge role in a Viksit Bharat – all we need is a benign and a forward looking ecosystem to help them along.

KV Srinivasan
Executive Director and CEO, Profectus Capital

Foreword

Integrating Digital Public Infrastructure with AI & ML to build a financially inclusive ecosystem

As we embrace a digital future, Artificial Intelligence (AI) and Machine Learning (ML) are transforming financial services. These advances enhance operational efficiencies, drive financial inclusion, reach underserved communities, and foster global economic empowerment.

Central to this transformation is India Stack, a groundbreaking digital infrastructure initiative demonstrating the power of digital public infrastructure in driving financial inclusion. India Stack comprises components such as the Unified Payments Interface (UPI), Aadhaar-enabled Payment System (AePS), eSign, Digital Identity Verification (eKYC & Video KYC), Digilocker, Account Aggregator and the Open Network for Digital Commerce (ONDC). ONDC enhances financial inclusion by integrating small and medium enterprises into the digital economy, providing them with broader access to financial services and markets. This integration facilitates secure transactions, democratizing access to financial services and e-commerce. When AI and ML integrate with India Stack, their effectiveness magnifies, ensuring marginalized communities benefit from modern financial services and e-commerce opportunities, fostering greater economic empowerment and inclusivity.

Building on this secure and accessible foundation, financial institutions must navigate an increasingly complex regulatory landscape, a challenge addressed by RegTech, or regulatory technology. RegTech solutions, powered by AI and ML, provide the tools necessary for financial institutions to maintain compliance effectively. AI-driven systems can monitor and interpret regulatory changes in real-time, ensuring compliance across multiple jurisdictions. The integration of Generative AI enhances these systems by generating insights and identifying efficiencies that streamline compliance processes. This adaptability reduces the risk of non-compliance and lowers operational costs, allowing financial institutions to focus on customer-centric innovations.

With robust digital public infrastructure and effective regulatory compliance frameworks, the lending sector is poised to benefit significantly from AI and ML. Traditional lending processes often exclude individuals without a formal credit history. However, AI-powered alternative credit scoring models analyse vast data, including transaction histories and non-traditional indicators, to assess creditworthiness. Generative AI refines these models by creating new methods for evaluating data, resulting in more accurate and inclusive credit assessments. By combining AI-driven lending models with digital public infrastructures like India Stack, financial institutions can extend credit to previously unbanked or underbanked individuals, fostering economic growth and reducing poverty.

Beyond conventional financial services, the development of the metaverse represents a significant advancement in customer engagement. The metaverse is a virtual space where users interact with digital environments and services. In the financial sector, it promises to revolutionize customer engagement and service delivery. Financial institutions create immersive experiences that simplify complex financial concepts, making them accessible through virtual banking branches and interactive financial education modules. The integration of AI, ML, and the metaverse is expanding the reach of financial education and services, making them more accessible to everyone.

While AI has its benefits, it is crucial to ensure its fair and ethical use, avoiding biases and bolstering trust and confidence.

Kiya.ai is at the forefront of this transformative wave. With a vision for an innovative and inclusive future, Kiya.ai leverages India Stack to redefine banking norms and drive financial inclusion. Its advanced AI solutions and accessible metaverse platform, Kiyaverse, empower global financial institutions to engage with diverse audiences. Aligned with Prime Minister Narendra Modi's initiative to promote inclusive technology, Kiya.ai is committed to preparing the banking industry for an AI-driven future, ensuring that innovation and inclusivity go hand in hand.

Rajesh Mirjankar
Managing Director and CEO, Kiya.ai

Executive summary

With a robust ecosystem, the domestic financial system recorded strong growth in FY24. The demand for faster turnaround times, immediate disbursement, better customer experience and custom products are driving end-to-end digitisation, creating pathways for collaboration with innovative fintech companies. This union fosters growth in digital inclusion, unified citizen experience, enhanced service delivery, digital transformation, data-driven decision-making, crisis response and resilience.

Digital public infrastructure, such as the Open Credit Enablement Network (OCEN) built on the India Stack, Open Network for Digital Commerce (ONDC), Account Aggregator framework (AA) and Unified Payments Interface (UPI), has revolutionised credit. It will continue to dominate the lending landscape over the next year. Banks are also revamping customer journeys and developing sustainable financing products with fintech firms.

Banks and NBFCs will be crucial in propelling India towards its vision of achieving a Viksit Bharat. With the rise of GenAI and open APIs, institutions must balance innovation with solid risk management systems that address cyber risks, protect personal data and ensure regulatory compliance.

As of 2022, India was the 10th-largest insurance market globally. It is expected to become the 6th-largest by 2032. Indian insurance companies can play a pivotal role in bridging the financial gap and contributing to a genuinely inclusive Amrit Kaal. This growth trajectory reflects emerging trends, such as customer-centricity, technology adoption, collaboration with Insurtech platforms, talent development and social responsibility.

The booming insurance sector is also facing significant shifts in regulatory, customer, product and digital advancements, such as competitive pricing, seeking potential investors, revamping digital strategy and cyber threats. The insurance industry envisions an empowered future with financial inclusion, and ensuring access to essential financial services, such as insurance, remains critical to fulfilling this vision. Strides such as "Jan Dhan Yojana" have helped fill some gaps by including millions of Indians who were earlier financially excluded, particularly in rural areas and among vulnerable groups.

Indian insurance companies have many opportunities to explore new business models, pursue mergers, embrace future changes and cutting-edge technologies, and strengthen internal regulations and governance procedures. These companies can target the rural populace using digital platforms and vernacular communication to implement inclusivity across levels. Collaborating with self-help groups, PM Yojna, and microfinance institutions can help reach marginalised communities and promote financial literacy campaigns that build awareness and trust.

India's asset management industry is vital for individual wealth creation and corporate growth. It offers diverse investment tools for long-term financial security and acts as a gateway to critical capital for businesses.

Retail participation increased, with retail investors comprising ~91 percent of the total 17.8 crore mutual fund folios, with the balance held by institutional and HNI investors. Equity-oriented schemes rose to 58 percent of industry assets in April 2024, followed by debt-oriented schemes at 15.9 percent. The asset management industry is experiencing emerging trends, including financial inclusion, technology adoption, theme-based portfolio construction, and increased accessibility. Asset managers need to collaborate with players inside and outside the financial industry to create innovative products, expand distribution and acquire new platforms as big players dominate the mutual fund market. Despite challenges such as government controls and operational costs, the asset management sector offers promising opportunities as it remains under-penetrated compared with global standards.

Firms should invest in financial education, create innovative product designs, collaborate with digital distribution channels, build infrastructure for B30 distribution, focus on retail investors, digitise their value chain, embed regulatory technology solutions and create environmentally positive products. With an ambitious target to cross INR100 trillion in AUM, the asset management sector will play a pivotal role in achieving India's vision of Amrit Kaal.

FSI overview: Banking

Current status

The domestic financial system witnessed strong growth in FY24, expanding in size and nurturing a robust ecosystem. Credit grew in double digits and was primarily driven by retail and MSME credit. There was an improvement in asset quality for Scheduled Commercial Banks (SCBs), with the Gross Non-Performing Assets (GNPA) ratio declining to a multi-year low of 3.2 percent and the Net Non-Performing Assets (NNPA) ratio to 0.8 percent in September 2023.[1] The Return on Assets (RoA) and Return on Equity (RoE) ratios increased to 1.2 percent and 12.9 percent, respectively.[2] The banking sector witnessed a Robust Capital to Risk-Weighted Assets Ratio (CRAR), and the NBFC sector witnessed a CRAR of 27.6 percent and a GNPA ratio of 4.6 percent in September 2023.[3]

The regulatory sandbox has encouraged a high level of innovation, including in the underwriting and lending space. The new Public Tech Platform for Frictionless Credit (PTPFC) that the Reserve Bank of India (RBI) launched in August 2023 for agriculture and small-value MSME loans has seen a significant offtake. PTPFC could be extended to other products. The fintech ecosystem continued to expand with segments of digital lending, payments, data-decisioning and SaaS applications. Digital public infrastructure such as Open Credit Enablement Network (OCEN) built on the India Stack, Open Network for Digital Commerce (ONDC), Account Aggregator framework (AA) and Unified Payments Interface (UPI) are revolutionising credit and will continue to be dominant forces in shaping the lending landscape over the year ahead.

There has been concern over the system's growing unsecured retail and credit card advances by commercial banks, NBFCs and fintech firms. The RBI recently tightened capital norms (increase in risk weights of 100 percent to 125 percent for unsecured personal loans and consumer durable loans and from 125 percent to 150 percent for credit cards) to address this risk build-up in the system. This includes personal loans but excludes loans for housing, education, vehicles and loans secured by gold. It also excludes microfinance loans extended by NBFCs.

Moreover, regulatory concerns regarding fintech and startup firms have been increasing. The finance ministry has urged regulators to conduct monthly meetings with fintech and start-up firms to address any concerns they may have and ensure regulatory compliance.

Emerging trends

The following few key shifts are visible due to newer risks and the changing landscape of the Indian banking and lending industry.

- **End-to-end digitisation and ecosystem buildout to drive efficiency**
  The banking and lending sector is undergoing a rapid transformation in terms of end-to-end digitisation due to growing customer demand for faster turnaround times, immediate disbursement, superior customer experience and custom products that meet their goal.

  Legacy players are collaborating with innovative fintech across the lending value chain: customer onboarding, data-analytics-rich loan management systems, fraud detection, KYC, early warning signals and digital collections, regulatory compliance and cybersecurity. Digitisation is bringing about efficiency in terms of both enhanced processes and cost.

- **Customer-centricity and hyper-personalisation with data-driven decisions**
  Banks have started shifting away from product-

[1] RBI Financial Stability Report, Dec 23 - Chapter II: Financial Institutions: Soundness and Resilience (Pg 66)
[2] RBI Financial Stability Report, Dec 23 - Chapter II: Financial Institutions: Soundness and Resilience (Pg 71)
[3] RBI Financial Stability Report, Dec 23 - Chapter II: Financial Institutions: Soundness and Resilience (Pg 87)

based business models to more customer-centric organisations. Products are getting more customised and targeted, enabling better customer experience and lower acquisition costs. Banks are investing in revamping customer journeys based on customer persona and hyper-personalisation.

Machine learning (ML), predictive analysis, speech analytics and Natural Language Processing (NLP) are some technologies banks are using to record their clients' profiles and attitudes during phone, in-person and digital encounters to derive the Next Best Action (NBA) for them.

Availability of data through open Application Programming Interfaces (APIs) and Account Aggregator (AA) is also benefiting the lower end of the pyramid, where additional New-to-Credit (NTC) customers that were left out of the formal funding channels can now be evaluated. The rise of data analytics (other than the traditional metrics of credit history and collateral) is critical in assessing the financing of the large, underpenetrated MSME segment that typically lacks documentation and credit history. (MSMEs contribute ~30 percent[4] to GDP, and currently, only 250 lakh MSMEs of the 630 lakh MSMEs[5] are funded through formal channels).

- **Rise of Banking-as-a-Service (BaaS) and embedded finance**
  Banks are rolling out their API stacks to third-party players to build new consumer-facing and enterprise-facing financial solutions. This allows banks to expand in the ecosystem and extend their customer reach.

  Banks are venturing into other industries by integrating financial products into non-financial products and services. In the retail sector, the rise of e-commerce giants, such as Amazon, Flipkart and Myntra, coupled with bank-fintech collaborations, has revolutionised Indian shopping habits. Embedding financing in these everyday interactions has unlocked new revenue streams for banks, expanding credit access and boosting purchasing power for millions.

- **Payment's modernisation and monetisation**
  Since its launch in 2016, UPI has helped India make remarkable strides in creating transparency and furthering the agenda of financial inclusion in the country. Launched in 2022, UPI Lite will further accelerate transaction volumes and help alleviate the load on banks' core systems. Players will now also look at monetising payment data.

- **Focus on sustainability**
  The financial sector plays a vital role in sustainability in terms of ensuring social and financial inclusion and achieving India's vision of net-zero (through sustainable climate funding and investments). Banks are looking at ways to support green financing and create new products with new-age fintech firms to promote sustainable financing. Advanced data management and analytics will be needed along with physical reach on the ESG front, given the need to collect and work with large amounts of structured and unstructured data. There are some emerging solutions that assist with data collection and ESG dashboards/reporting and analytics.

[4] Press release on Role of MSME sector in the country (https://pib.gov.in/PressReleaseIframePage.aspx?PRID=1946375)

[5] Per the MSME pulse report (Feb 2024) - Of the 630 Lakh MSME corporates in India, only 250 lakh are included in the formal credit ecosystem i.e. ~40 percent MSMEs are funded through formal channels

Current challenges

As the banking industry continues to grow, the following are a few imminent challenges the banking industry will face:

Legacy systems

Banks will have to consider the cost implications of adopting newer technologies, i.e., enable API integration with new- age fintech firms and third parties and introduce new products and custom experiences. They will need to rethink digital strategy to improve consumer journeys. To enable BaaS, for instance, banks will need to modernise their core systems. Enabling API integration for each banking functionality is a tedious and investment-heavy requirement. Banks would also have to invest in modernising the tech stack and using modular architecture, such as microservices. In addition, real-time updates (as opposed to the legacy batch processing systems) would be required.

Talent acquisition/upskilling in technology

Given the rapid digital transformation in the banking space, talent acquisition and upskilling will be important. Banks will need to invest significant time and money in hiring and upskilling talent across data science, cybersecurity, User Interface/User Experience (UI/UX) developers, risk management and hyper-personalisation. Banks will have to hire senior people from other domains for digital transformation.

Fraud and cybersecurity

Continuous advancements in information technology are leading to a shift in data from physical and on-premises to digital and cloud storage. In addition, with the launch of open banking and the proliferation of data sharing with third-party apps, data breaches and fraud need close monitoring, and systems require regular upgrades to detect them promptly.

In this era of digitisation and data sharing, banks must be prudent about safeguarding against malware, viruses and vulnerabilities stemming from cloud infrastructure, securing confidential data, payment frauds, ATM skimming and preventing risk of social engineering.

CASA (Current Account and Savings Account) pressure

The CASA ratio for Indian banks has been under pressure; overall deposit growth has also been under pressure. This can potentially affect banks' profitability and growth.

Data privacy concerns

Financial services companies must be seen as custodians of sensitive financial data. To balance innovation and data protection, India's first data protection act, the Digital Personal Data Protection Act (DPDPA), was released in 2023.

What does the future hold for the banking sector?

Banks and NBFCs will play a crucial role in propelling India towards its vision of achieving a Viksit Bharat 2047 by:

- Financing consumer credit that will likely fuel demand and promote growth in the economy
- Promoting financial inclusion to achieve cost-effective last-mile credit penetration through technology and collaborating with innovative fintech firms across the value chain
- Financing key sectors, building manufacturing capacity and developing large-scale infrastructure
- Financing green/ sustainability initiatives

Some of the key trends that will play out (a few of which are already underway) are mentioned below:

- End-to-end digitisation of lending, including smart loan origination platforms and smarter credit decisioning through better data analytics
- Evolution of payment products, including new ways of monetiszation of payment data and infrastructure
- Generate revenue by using data and build smart platforms for cross-selling and promote banks to consider becoming multi-service platforms
- Transform corporate banking to cater to end-to-end corporate banking needs, including omnichannel experiences and seamless integration using B2B APIs with corporate ERP systems, enabling flexibility across banking and payment services
- Transformation in cross-border payments—UPI-led and other innovations
- Move towards hyper-automation, particularly AI/GenAI-led, to reduce costs/increase operational efficiency
- Promote cloud adoption through tech and data stack modernisation and microservices-based architecture
- Embed regulatory technology solutions (including cybersecurity) for real-time monitoring and analysis of potential compliance and risk management
- Launch new platforms and products for sustainable financing that lead to a positive environmental impact

Banks and lending institutions have an interesting journey ahead and will play a critical role in achieving India's vision of Viksit Bharat. Institutions will have to balance innovation with strong risk management systems that address cyber risks and personal data protection to ensure regulatory compliance.

FSI overview: Insurance

Current status

The Indian industry is on a fast growth path. Economic growth, an expanding middle class, innovation and regulatory support are driving insurance market growth. As of 2022, India was the 10th largest insurance market globally and is expected to become the 6th largest by 2032.[6] The insurance sector in India is expected to record the fastest growth (vis-à-vis other G20 countries), with total premiums projected to rise more than 7 percent in real terms during the 2024-28 period.

Emerging trends

With newer risks to tackle and the changing landscape of the Indian insurance industry, the following few key shifts are visible:

Preventing losses and becoming more customer-centric: The industry is adopting a proactive approach to risk management, focusing on preventing losses before they occur. This includes using data analytics and AI to identify and mitigate risks and developing new customer-centric products and services that help customers avoid losses.

Technology adoption: Insurers are adopting new technologies, such as predictive modelling for triage models and Artificial Intelligence (AI), ML and GenAI, to improve their operations and customer experience. For example, they use AI to increase STP by automating underwriting and claims processes, ML to develop personalised insurance products and GenAI to enhance customer experience and reduce mis-selling.

Mergers and acquisitions: A trend of consolidation in the insurance industry is seen as insurers look to gain scale and efficiency. This is driven by factors such as the increasing complexity of the regulatory environment and the need to invest in new technologies via collaboration with InsurTech companies. This can up the game in distribution, policy issuance, etc. A notable trend is the surge of foreign players increasing their stakes in the Indian joint venture entity, attributed to recent regulatory changes allowing 74%.

Talent acquisition: The insurance industry faces a talent shortage as it competes with other industries for skilled workers. Insurers are investing in talent acquisition and development programmes to attract and retain top talent. The influx of talent from other industries to insurance will hopefully push the innovation quotient in the industry with fresh perspectives.

Regulatory changes: The DPDP Act, 2023, will reshape the insurance industry, given the large volumes of personal data Insurance companies and allied industries deal with. In addition, players in the insurance ecosystem (such as brokers, corporate agents, TPAs.) must protect data from unauthorised access and strengthen existing corporate governance in their organisations. Another big trend is in adopting the IFRS 17 standard which is a complex process requiring time and bandwidth from the management.

Sustainability and social responsibility: Insurers focus on sustainability and social responsibility as these issues become more important to customers and investors. This includes investing in renewable energy and developing products and services addressing social issues, such as climate change and income inequality. These are real challenges, especially for India, as claims pay-out is increasing due to climate changes, and increased penetration is reducing the uninsured losses for the country. Companies are adopting modern risk management principles to ensure they can price it appropriately.

[6] IRDAI Annual report (Pg 203)

Current challenges

The Indian insurance industry is facing significant shifts in regulatory, customer, product and digital advancements. The industry is experiencing several important changes, such as:

- IRDAI plans to achieve its "Insurance for All by 2047" vision.
- Higher focus on accounting standards of IFRS17 and risk-based supervision on the anvil. New acts/notifications on the DPDP Act, 2023, surrender value, EoM and customer centricity and, master circulars are on the rise. This will require investments and incur costs for companies.
- Need for companies to outsmart their competition by adopting digital strategy and transformation to improve consumer (acquisition, interaction and engagement), product and channel strategy and operations through technologies such as AI/ML and data infrastructure is on the rise.
- Cyber threats can potentially affect data protection, infrastructure, and processes.

What does the future hold for the insurance sector?

The insurance industry's prospects look promising, and India's roadmap to 2047, or "Amrit Kaal", as it is called, envisions an empowered and inclusive economy. Financial inclusion, ensuring access to essential financial services, such as insurance, remains critical to fulfil this vision. Strides such as Jan Dhan Yojana have helped fill some gaps by including millions of Indians who were earlier financially excluded, particularly in rural areas and among vulnerable groups. India's insurance density is low at US$92 (premium to total population ratio) compared with the global average of US$853.[7] Limited awareness, affordability and product accessibility hinder wider insurance penetration.

IRDAI's vision of "Insurance for All by 2047" is based on the following key tenets:

01 Strong economic growth and rising disposable income

02 Favourable demographics with a young population

03 Increased risk awareness post COVID-19

04 Increased digital penetration due to social media usage, smartphone adaption and surge in digital services

05 Regulatory developments and Government support

[7] IRDAI Annual report (Pg 204)

Indian insurance companies hold immense potential to be a key part of IRDAI's vision. They have a lot of opportunities to:

- Explore new business models, digital expansion or collaborations with the ecosystem; pursue mergers, acquisitions or foreign direct investment; and re-evaluate current distribution strategies
- Embrace future changes and regulations by adopting new global standards while maintaining rigorous compliance
- Use cutting-edge technologies and digital transformation, translating technology to process gains, direct customer impacts, product innovation and the potential to be the first mover in realising future-driven possibilities
- Mitigate modern cyber threats by staying updated on cyber best practices, addressing reputational damage risks and strengthening internal regulations and governance procedures

However, for a fully inclusive programme, there are different options insurance companies can take to reach the rural populace and vulnerable groups:

Using technology

Digital platforms and modern core platforms with vernacular communication can simplify access and overcome some geographical barriers. Also, for areas such as crop insurance, technology can be used to make the claims process seamless.

Collaborations

Collaborating with self-help groups, PM Yojna and microfinance institutions can reach marginalised communities.

Financial literacy

Promoting financial literacy campaigns can build awareness and trust in insurance products.

FSI overview: Asset management industry

Introduction

India's asset management industry is a crucial component of its financial system, driving both individual wealth creation and corporate growth. It empowers individuals with diverse investment tools, paving the way for long-term financial security. For businesses, it acts as a gateway to vital capital, deepening the equity and debt markets. This not only unlocks new funding sources but also fosters responsible corporate governance practices, strengthening the overall financial landscape.

Current state

Around 44 asset management companies operate in India, categorised into private-sector mutual funds, bank-sponsored mutual funds and mutual fund institutions. Out of the total 44 AMCs, 37 are privately owned, six are bank-sponsored, and an institution operates one. Overall, there was a growth of ~37 percent (since April 2023), with the total mutual fund Assets Under Management (AUM) at the ~INR57 lakh crore mark as of April 2024.[8] Retail participation increased, with retail investors comprising ~91 percent of the total 17.8 crore mutual fund folios, with the balance held by institutional and HNI investors (as of March 2024).[9] This was driven by the adoption of digital channels for distribution to retail investors and favourable regulatory changes, some of which included the reduction of the Total Expense Ratio (TER), measures to promote transparency for investors and commission guidelines.

The proportion of equity-oriented schemes increased to 58% of industry assets as of April 2024.[10] Debt-oriented schemes were the second largest category, with a 15.9 percent share of the total assets, followed by 13.2 percent in the liquid and money markets and 12.8 percent in ETFs (Exchange Traded Funds) and FoFs (Fund of Funds).[11] Total outstanding Systemic Investment Plan (SIP) accounts stood at 8.7 crore, and monthly SIP inflows crossed INR20,000 crore in April 2024.[12] 18 percent of the mutual fund assets as of April 2024 came from the B30 locations, with equity being the major asset group in the total assets.[13]

As of 31 December 2023, INR10.8 lakh crore of commitments and INR4.29 lakh crore of funds were raised across the Category I, II, and III Alternative Investment Funds.[14]

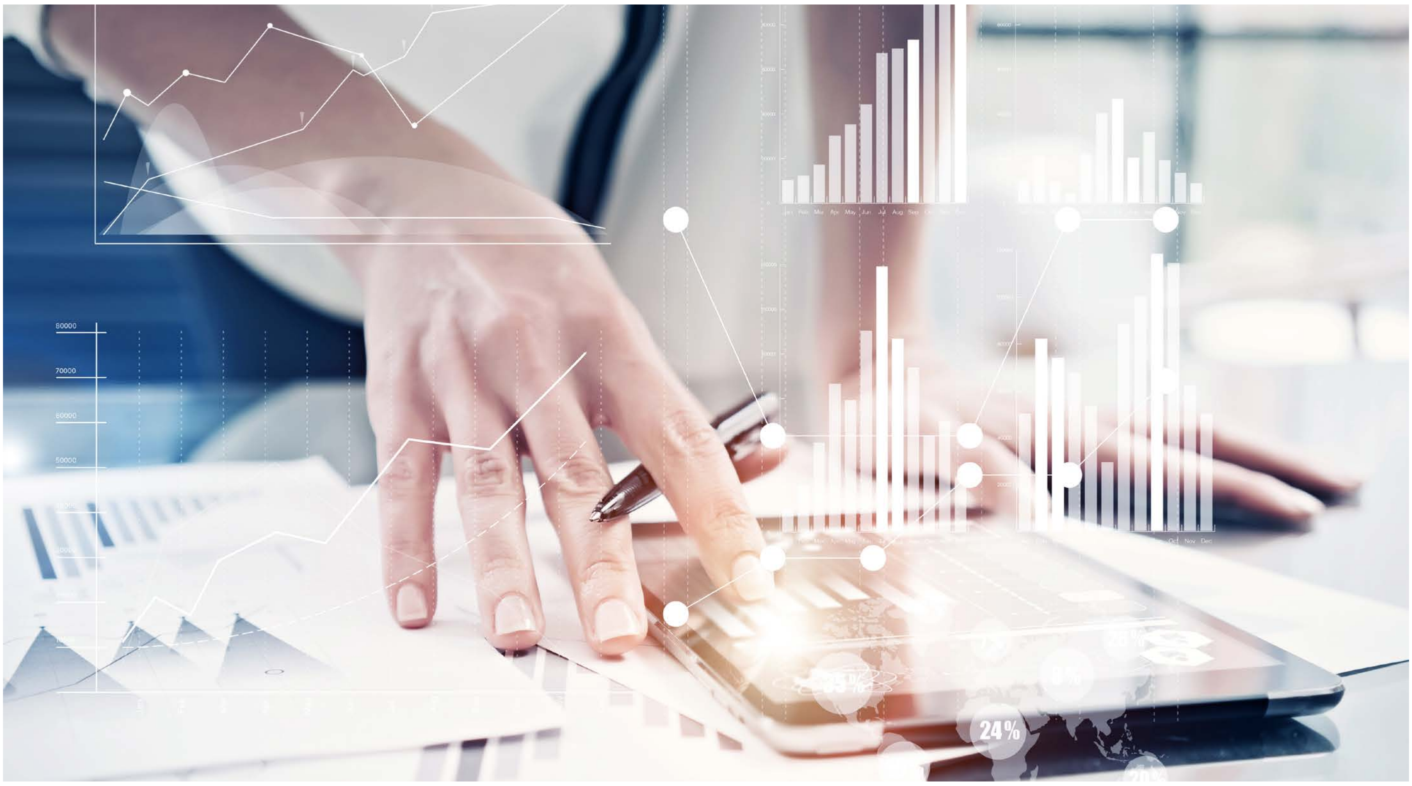
Big players continued to dominate the mutual fund market due to their strong distribution capabilities. Scale and robust distribution capabilities remain key drivers for sustainable growth in the space. In April 2024, Hinduja Group entered the mutual fund space—IndusInd International Holdings invested a majority stake in Invesco India Asset Management Limited. With increasing competition and the entry of new players in the space, the industry could see further consolidation.

The mutual fund industry body AMFI is eyeing a tenfold investor base growth, aiming to reach 10 crore investors and cross the INR100 lakh crore AUM mark by the turn of the decade. This will primarily be driven by three distinct categories of market expansion—Distribution outreach, inclusion of middle-income households through simplification and digitalisation and a higher share of individual savings.

Emerging trends

1. **Push towards financial inclusion through increased accessibility and reach**
   - Penetration of user-friendly mobile apps and online platforms offered in local languages, largely by discount brokers.

[8] AMFI Industry trends report (Pg 1)
[9] AMFI Folio and ticket size industry analysis (Pg 1)
[10] AMFI Industry trends report (Pg 2)
[11] AMFI Industry trends report (Pg 2)
[12] AMFI Industry report
[13] AMFI T30 v/s B30 industry analysis (Pg 1)
[14] SEBI



- Offering micro-investment products to the masses, such as the INR500 monthly mutual fund SIPs. There are discussions to bring this down further to INR250 to increase retail participation and promote financial inclusion.
- Inclusion through simplification of products and customer onboarding journeys.

2. **Theme-driven portfolio construction**
Theme-driven portfolio construction is gaining prominence as a vehicle for product development. Globally, sustainability as a theme is dominant and ESG-focused funds (Environmental, Social and Governance) are growing in importance. In India, the ESG theme is also gaining popularity, and a few fund houses have launched ESG-thematic funds. Given the rise of data-driven tools and analytics, ESG impact can also be measured more efficiently. Sectoral and theme-driven investing is poised to rise, with sectors such as infrastructure, banking, pharmaceuticals/healthcare and manufacturing being some of the pivotal sectors over the next decade.

3. **Adoption of technology**
Globally, technology is driving personalisation of product offerings and customer experience across industries and companies.

i. Product offerings
There is a visible shift in the investment landscape with the rise of:

- Tech-savvy and younger investors, who are looking for appealing digital platforms with user-friendly interfaces.
- Increased access to the masses with innovative products offered digitally with lower minimum investment requirements and fees.
- Need for tailored solutions and stock-picking through algorithmic-based recommendations based on individual needs and risk profiles.

ii. Customer service
In addition to new client acquisition, retaining clients in a highly competitive market remains key. To ensure client loyalty, fund houses will have to adopt technology and build platforms that offer superior customer service, including faster onboarding, online transaction capabilities, better customer grievance resolution, efficient and timely dashboards for client reporting that include real-time data and analytics. Close collaboration and seamless integration between the front, middle and back offices of the companies, including the finance, technology and security teams will be required to deliver this.

4. **Ecosystem play**
Traditional asset managers will have to collaborate with players in the wider financial services industry and outside to create innovative products that would lead to deeper penetration and wider distribution. Partnerships and collaboration will be required for new customer acquisition, widening distribution capabilities in tier 3 and tier 4, and acquiring new capabilities and platforms.

Current challenges

1. **Creating robust distribution**
Despite the large growth in AUM, penetration remains a challenge. While urban cities have witnessed stronger participation, there is still a substantial gap in smaller cities and rural areas. One way to address this would be financial literacy and education. While the industry is allocating funds for investor education, educating the masses about mutual fund investing is still insufficient.

   Increased penetration can also be addressed by increasing the number of distributors, building distribution capabilities for B30 and creating standard APIs for collaboration with fintech to assist with digital distribution capabilities. In addition, custom products and strategies to address unique investor preferences outside urban centres may be required.

2. **Governance controls and risk management**
With the increasing use of data-driven models and analytics, cybersecurity risks and appropriate risk mitigation tools will need to be deployed. To effectively manage risks, seamless integration among the front, middle, and back offices is essential.

3. **Operational and cost challenges**
Although the mutual fund industry has made considerable progress in standardising processes, a few challenges persist. These include simplifying the KYC procedures to ensure hassle-free onboarding, allowing Aadhaar to be used interchangeably with PAN, and enabling investments based on "Bank KYC".

   Firms will also need to invest in marketing, customer acquisition for B30 expansion and keeping up with the constantly evolving regulatory changes.

What does the future hold for the asset management sector?

In 2024, the asset management sector faces a blend of promising opportunities, pressing priorities and factors demanding careful consideration. With intense competition for AUM, asset management companies actively seek ways to differentiate themselves, particularly in emerging technologies, talent development, client relations and ESG initiatives.

Despite remarkable progress, the Indian asset management industry remains significantly under-penetrated compared to global standards and other financial services. Limited product penetration, especially in B30 cities where most Indian households reside, along with low investor awareness, underscores the substantial growth potential in the industry.

The asset management sector will play a key role in achieving India's vision of Amrit Kaal, and firms will need to:

- Invest in financial education for investors, particularly at the bottom of the pyramid, to broaden investor outreach and increase the financialisation of savings.
- Innovate in product design to cater to newer customer sets, such as the millennials and digital-savvy customers.
- Collaborate with digital distribution channels within the financial services space and outside for customer acquisition and product innovation.
- Build and invest in infrastructure for B30 distribution.
- Focus on SIPs, which have gained popularity among retail investors.
- Digitise the value chain by using analytics-driven models to provide product personalisation of better alphas, portfolio monitoring tools, real-time dashboards and automated risk management.
- Embed regulatory technology solutions (including cybersecurity) for real-time monitoring and analysis of potential risks regarding compliance and risk management.
- Create new products that lead to a positive environmental impact.

AMFI is expecting to cross a target of INR100 trillion in AUM in the next few years. This growth trajectory presents immense opportunities for the industry to fulfil its role as a key driver of economic growth and financial inclusion in India.

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