Emerging Paradigms in Banking Leadership[1]

At the outset, I would like to thank CAFRAL and CEEI for giving the opportunity to be part of this significant event, with curated contents through the week-long engagements.

Discussing the emerging paradigms as an opening bell is not an easy task. In a 2001 book titled 'Mind the Gaffe - a Guide to Common Errors in English', author Larry Trask advised caution when reading anything that contained the phrase 'paradigm shift', hinting the abuse and overuse of the term. In the context of banking leadership, the term 'paradigm' would rather diverge from its technical or rhetorical meaning and stay close to its Greek origin, which meant 'pattern'. The steadily progressive evolution of the concept of banking in 8000 BC is likely to have entered the modern banking era in 1492[i] in the world and in 1683[ii] in India. Banks have continued to remain fundamental and essential to an economy over centuries. The so-called 'disruptions' to the business of banking at different points have been well soaked up, like effect of stones thrown into a deep lake that established Archimedes' principle. This has been possible mainly by the leaderships who have steered banking during their incumbency and passed on the legacy to new leaders, mainly through a process of osmosis. The well-known fiduciary responsibility of the bank confers a premium on good governance and prudence, with natural accompaniment of a high degree of regulation. That, in turn, casts a spotlight on leaderships which not only drive single banks but collectively drive the banking system and through that, a crucial part of the real economy.

2. Leadership, at an operative level, could be defined as influence[iii]. Long before professional banking leaders descended on the scene in India, there were indomitable banking families with influence of a kind. There was the family of Seths in early 18th century, who were given the title of 'Jagat Seth' by the British going by his influence. Historical accounts state that their business brushed shoulder with that of Bank of England in terms of importance; their wealth topped that of the British economy in 1720s and they had more cash than that of all of the England's banks put together. That may all be 'native' water under the bridge now but provides a rich contrast to

[1] **Keynote address by Jayant Kumar Dash, Executive Director, Reserve Bank of India at Financial Sector Leadership Program of CAFRAL on February 5, 2024.**

modern Indian banking leadership and discourses. We have seen iconic leaders in the banking space, both internationally as well as in India. Let me try to triangulate a frame of reference for emerging banking leadership in terms of (i) a critical view on the present leadership; (ii) select ‘paradigms’ on the horizon and (iii) leadership pipeline for Indian banks; all without using the words ‘inflection point’ or ‘in the cusp of’.

Banking Leadership in India

3. The present financial robustness of Indian banks speaks volumes about the positive contribution by its leadership. The stereotypes of banking leadership in India have unmistakably changed with cross motion among public and private sectors as well as domestic and foreign banks, supplemented by active policy substructures. Nonetheless, some critical view would not be out of place to spur a discussion. As for universe of common leadership styles taught in leadership programs, Indian banking leaders seem to have generally graduated from the *laissez faire*, transactional or bureaucratic styles. However, directive / authoritative style, albeit in receding numbers, might have affected a desirable conduct environment in a few cases. This at times touches the functioning of an independent board. Transformational or strategic leadership traits demonstrated by iconic leaders remain bounded. The narrow use of leadership styles often create limitations in critical thinking for a structured response or a differentiated playbook for the dynamic financial marketplace.

4. A noticeable bias among some bank leadership teams can be described as hivemind traits, wherein analogous strategies for commoditized financial products and services are adopted. The default or drifted business approach, rather than brainstormed or differentiated, often tend to be presented as strategies in some cases. Risk management effectively front runs risks rather than halting its spiral. Without generalization, it is often pointed out that the emotional intelligence (EI) profiles of banking leadership continue to lag that demonstrated in other industries. EI, which envelops understanding, empathy, and the ability to influence, is often treated with higher importance then cognitive ability in anticipating outstanding leadership performance. Leadership bereft of EI tends to develop blind spots that affect ability to lead transformation or sustain changes achieved. Have we seen that?

The Rising Paradigms

5. The new matrix of banking paradigms from leadership perspectives that are widely discussed are not hard to spot. The dialogues in recent WEF at Davos among banking leaders echoed some notions of “uncertainty” and ‘resilience’ as they deliberated on ways to deal with an array of budding disruptive scenarios arising from elevated degree of macroeconomic, technological, geopolitical dislocation. As leaders aspired to transform adversities to opportunities, the common threads ran along visualizing and bracing for “crucible moments” and taking pivotal decisions that can shape the future trajectory of banking. There was an easy unanimity that the complexion of emerging risks likely to come in the way during next decade could be different from that of the gone-by decade. Shape of such risks arising from within the banking / financial system have been seen in the forms such as the risk of rapid-fire deposit runs on digital rails, increased interest rate volatility, spill-over risks from non-systemically important entities’ clusters. Risks emanating from outside the system such as geopolitics, newer sources of operational risk and climate change need effective tackle by the leadership without having the benefit of past learning. In the spirit of today’s conference, I will outline some of the emerging challenges to banking leadership in India that could float on surface for some time to come.

Accelerating Disintermediation and Non-bank competition

6. The fundamental-most role of banks in financial intermediation in the economy is being upended with slow but sure shifts. On the asset side, banks’ share of financing a fast growing real economy is slowly dwindling as non-bank financial markets and other private funding sources make moves. Acceptance by silence of this shift might partly owe it to incremental prudential regulations for bank safety as well as the certain repairs and deleveraging of bank balance sheets. The asymmetry of such considerations on the challenger side could smell of arbitrage and return as risks to banking leadership through transformed channels, unless extrapolated now for strategic steps. Some of the market based products could be masked credits with reduced or lagged visibility of risks. From being the direct catchment of entire liquidity in the system, the banks now have to deal with a layer of liquidity managing financial and non-financial intermediaries. On the liability side, the banks have been affected by the shift of saving preference by households and growth of newer financial intermediaries. This is apparent from tell-tale RBI data[iv]. Whereas change in

household assets in bank deposits fell to ₹7.79 trillion in 2021-22 from ₹12.01 trillion the previous year, assets in shares and debentures went up to ₹2.14 trillion from ₹1.07 trillion during the same period. Share of bank deposits in GDP current price) declined to 66.24% in 2022-23 from 70.15% the previous year. The CAGR of average AUM[v] in MFs between December 2019 (₹27.26 trillion) and December 2023 (₹51.10 trillion) was 17.01% whereas that for bank deposits between March 2019 (₹125.74 trillion) and March 2023 (₹180.44 trillion) was 9.45%. If juxtaposed against the institutional vantage of the banks and MFs, the gradients would be amplified for the banking leaderships to ponder but that will be only part of the challenges. It is interesting to observe that very bank employees sell third party and insurance linked investment / endowment products to bank depositors for the incentive mechanism put in place by third parties. If India, a traditional nation of savers, lunges into becoming a nation of investors, what strategy the bank leaders hold, other than dialling up the deposit interest rates?

7. While banking RoAs / RoEs have inched up recently, there are trends that pose downward pressure on banking profitability over coming period. The need to call it a paradigm arises from the need for bank leadership to approach it from outside the interest rate playbook. The NII staple is already dealing with compression due to cost bumps and dents on credit yields due to the competition and partnership factors rather than usual rate-cycle dynamics. Apart from the structural shift mentioned earlier, the secular displacement of operational incomes caused by FinTech / Payment technology companies are widely discussed. The progressive disintermediation of financial services, growing customer awareness, and regulatory stress toward transparency and fairness of charges and fees could also lead to earthward bias in fee incomes. The challenge to banking economics from this side has important strategic implications. Both intensification and diversification of competition and a shift in the profile of talent are expected to lead to higher per-employee costs. Mitigation by technology-led transformation in sourcing, underwriting, operations, and support functions involving incremental operating expenses across banks, depending on their strategies around talent, digital transformation, and technology capex, are where the leaderships look now.

Macroeconomic conditions and global spillovers

8. Globally, the pressured NII reeling from slowing growth, interest rates uncertainty is no way helped by significant geopolitical uncertainty. The low interest rate environment created by central banks around the world to stimulate growth will have a prolonged negative impact on banks' businesses. Although the unusual environment supported borrowers' repayment capacity and creating benign funding conditions for banks, low interest rates may constrain the banks' NIMs and bottom-line profitability for some time to come. Moreover, rising compliance costs, enforcement / settlement penalties/ costs and high credit costs in many banking systems are further pressuring banks' bottom lines, though India remains an exception so far. Low earnings would trim internal capital generation and hence bank leaders are left to build up fresh capital that are enamoured of other better yielding financial service sectors. Optimizing both risk-weighted and nominal leverage to meet Basel III requirements are the other options but it may have second order impact on the economic growth. There are still a number of factors that could contribute to a regime shift characterized by structurally higher interest rate volatility. Vulnerability to stagflationary supply shocks from the rewiring of globalisation, geopolitical and political economy tensions, and energy shocks from climate change (and related policies) are factors banking leadership needs to reckon with. This contrasts with prior decades, where supply side developments of the economy were typically favourable for growth and inflation and so moderated financial market volatility.

9. One more factor, a derivative of macroeconomic developments, that banking leaders should be aware of is about the new challenging complexion that contagion risk is assuming. Systemic risks are now capable of arising from entities that individually are not systemically important. This owe it to the speed of money and information flows, which can magnify herding effects *a la* famous $E=MC^2$ and procyclicality in parts of the international asset management industry that have grown strongly.

Innovation and Digital Transformation

10. Jamie Dimon of JPMC had warned in a 2015 letter to the banks shareholder: 'Silicon valley is coming'. While Silicon Valley Bank might have read it wrongly, but innovation and digital transformation have remained a key paradigm for banking leadership all over. Digital leadership i.e thinking and acting like a digital company has

become an important part of strategy of more successful banks. This essentially translates into having a commensurate tech stack, making IT a part of business rather than just a support function, and optimising the use of internally & externally available data to understand customers. The growing spread of adept web and mobile based digital technologies and the rates at which existing and prospective customers integrate these technologies into their lives have eroded supremacy or near monopoly of the banks in the domains of certain traditional financial products. Falling transaction costs associated with modern digital technologies will continue to help customers or newer third parties process information and provide corresponding financial business services at a scale that very closely compete with banking. Yet, vision of many of the banking leaders suffered from certain degree of technology blind spots in the pivotal stage. Faced with increasing pressure of multiple performance and greater RoE, banking leaders were attracted by sales pitch of technology's claims of greater, faster and cheaper performance without a long-term digital strategy. This has caused what was perceived as enabling technologies turning destabilizing technologies. For banks to become part of the disruption of new digital services and not its victims, leaderships need to address the growing competition from FinTech in reimagined ways. Instilling a start-up mindset In a rapidly changing digital landscape is a leadership quality which has yielded transformational results by acting more like a technology start-up, and less like a bank. The most promising strategies focus on creating and fostering a culture within the existing organization that cultivates new ideas and products/services collaborating with newly emerging competitors or investing in such businesses very early on. The technology leaders may need to have the aspiration to shape the digital future for their banks founded on learnings from leading technology companies. For longer journeys, banks need to acquire broad-based set of digital capabilities.

11. Being a digital savvy leader is the first step to shift from a pure innovation mindset to strategic innovation. Much digitalization / data programs fail when the low-hanging fruits turn out to be entrapments when it is approached as IT projects rather than a bank-wide effort or a part of data architecture. First, many leaders need to realize that nothing is more fundamental than data quality before adopting digital innovation. Bad data was the norm across banks a few years ago. Secondly, without buy-in from all stake holders down to the grass root and not creating an effective organization structure often stumble the initiatives. Right investments in emerging technologies

result in growingly sophisticated customer experiences, including personalized interactions and tailored value propositions, as well as significant opportunities for clocking efficiency through automation. However, one needs to be careful about the emerging technologies hype cycle[vi] and not settling for optics such as that for AI/ML and rather do the hard work to make meaningful changes. Every innovation with emerging technologies must have an explicit goal to boost revenue, trim costs and mitigate risk – and at a scale that materially impacts earnings over a visible time horizon. Leaders must not only adopt digital technologies but also foster a culture that encourages experimentation and embraces disruptive innovations to stay relevant. It may require complete reimagination rather than mere de-frictioning that is in trend. Without establishing clear design principles, scaling and extension may prove to be a challenge going forward.

Collaboration and Eco System Thinking

12. Connected to above lines, banks must have a strategy for collaboration and eco-system thinking leadership. Despite evidence of the value of providing customers with services leveraging their own business's data, banks are not effectively responding to digital challenge. Accepting the fact that banks not being tech companies, knowing how to do this isn't intrinsic to them. This is largely because banks are trying to compete on tech's terms rather than being in a position to set out their own terms. Developing proactive strategies to get ahead of the fintech competition by generating intelligence from the abundance of valuable customer data that the banks own has not been adopted by many large banks. When it comes to data, however, process integration must come before intelligence, and this is where banks can probably find a way to compete on their own terms. Then banking leadership can begin to realize the unique position they have in the financial and business ecosystem, and how they could build solutions that capitalize on that position.

13. The banks adopting digital integration strategies to compete or collaborate with digital lenders at both low and high ends of integration as well as investments. At low investment end, the arm's length dealing (e.g buying loans or receiving references) need low integration and using of the online marketplaces offered by FinTechs or using their technology to source online applications seem to be the low hanging fruits. On the high investment ends, banks set up internal incubators or invest in other FinTechs

on low integration side and form white label arrangements or adopt build or buy strategy for FinTechs.

Customer Centric Leadership

14. Bankers taking pride in winning multigenerational loyalty of their customers are passé, along side many other things. Consumer behaviors are changing, shaped by their experiences with offerings across other non-bank industry leaders. Digital disruption has progressed to a point where switching banks is easy for customers, empowering them the power to unbundle financial service relationship. The traditional strategy of bank leadership to eye customer's full wallets, now competition for each product in a customer's wallet is stoked up, improving price transparency. This raises the potential for banks to be disintermediated and relegated to balance-sheet providers with limited returns on equity. It has been observed that in case of acquired assets from fintechs/ NBFCs, while the banks enjoy a minor mark-up, the entire upside margin is retained by the originators without any advantage to borrowers. What is more important is that the customers remain remote to the banks. It's clear that banks need to adopt new strategies to match the offer presented by digital-first and UX-driven payment platforms. The leadership needs to be focused on giving banks the tools they need to truly harness their data and transform their customer experience.

15. The fundamental dynamics that drive customer decision-making in most different industries are similar. Price, service, and trust are the key ingredients –trust being special to banking. Today, much of information is available from open source or comparison / aggregator portals, or in direct exchanges with experts on platforms. As a result, clients expect more customized / processed information and better-quality services from their banks than in the past. To remain competitive and profitable, bank leadership will need to adapt to these emerging client needs and behaviours. The core building blocks to lead through customer-experience transformations involves setting clear aspiration and purpose; deciding on the non-incremental transformation that is required for the business ; and enabling the transformation process.

Leadership Talent Development / Management

16. Talent is a top strategic objective of most banks. A bank's health is measured, not only by the financial and operational metrics around performance but also organizational health in terms of capability building and maturity forms. Capability

building is about not only helping employees train in the technical skills their job demands, but also ‘developing’ leadership and foundational management skills. Such capability building is especially critical in banking and mechanical financial investment in resources may be less important than time and commitment offered by top management to develop capable personnel. It is often alleged that banking leaderships perform poorly when it comes to employee engagement which manifested through high attrition in middle management becoming the new normal. An analysis of Linkedin data (June 2021 – June 2023) revealed that globally a typical bank loses four AI people for every five it hires.

17. While banking leaders recognize soft skills such as empathy, resilience, kindness, communication, etc. to be vital for effective management, there is often a typical belief that it is an innate trait of individual leaders. On the contrary, they are much more required to be honed through learning and development. It’s also good to be an outward looking organization welcoming have people from outside the bank come and challenge. It needs a lot of conviction to face ‘show me the money’ posers but culture continues to be only truly competitive point of difference beyond short term.

Risk Management & Regulatory Compliance

18. As the regulatory landscape unrolls, increasing focus on effective risk management and compliance are the most discernible undertones. Bank leaders are expected to be well-versed in regulatory requirements and implement robust risk management practices to ensure the stability and sustainability of their bank. In terms of non-financial risks, the most immediate and challenging of which is cyber risk. The scope for, and consequences of, cyber-attacks continue to grow bigger. Challenges are elevating from third-party technology dependencies, geopolitical tensions and resourcing constraints among smaller banks that could be weakest link of vulnerability for the wider system. The second operational risk relates to critical technology service providers that have been largely operating outside the financial regulatory perimeter and some of them do not have much competition. Banks and financial market infrastructures are considering moving some services to the cloud, albeit for good reasons. However, exposure is concentrated in a select number of service providers and an outage could hamper many critical functions across the board. Banks’ use of emerging technologies too raises concerns about their capability in governance, risk

management, platform concentration risk and responsiveness in a crisis. The third operational risk – artificial intelligence (AI) – does not seem that distant anymore and no less challenging. While offering boundless opportunities for the banking and financial system, managing the associated risks will not be anything like the risk management models is use by banking leadership so far.

19. One more dimension of risk management arises from the challenges in sustaining the process improvements brought about as a part of executing strategy which often tend to backslide after initial excitement period, as unseen sides unfold. It often dawns that consultants were telling only part of the story and as a result, some improvements sustain, and others do not. Without visible support from the board and senior leadership, frontline team members tend to believe waning of bank's enthusiasm leading to retrogression. Addressing the low hanging fruits is always easy for leaders; it becomes harder in the long term. Another troublesome hindrance to sustained improvement is initiative fatigue when banking leaders jump from one improvement fad to another or from high targets to higher targets. Banks all over the world will need to develop strategies to respond to these challenges. To address these issues, banks will have to adjust their businesses wherever possible.

Leadership in Sustainable Banking – Climate Risk

20. Risks to financial stability resulting from climate change and related policies will be with banks for years to come. Extreme weather patterns and higher average temperatures would result in physical risks that would negatively impact the value of assets and revenue streams in sectors and parts of the economy. Transition risks, including unexpected changes to regulations and consumer preferences, can also impact the value of assets or businesses in emissions-intensive industries as the belief that 'planetary risks deserve priority over financial risk' is widely ingrained.

Ethical Leadership

21. Leaders may need to embrace a more complex code of ethical behavior than they may ve learned in earlier managerial roles as ethical considerations are gaining paramountcy in the emerging paradigm. Banking leaders, in addition to adhering to regulatory standards, will have to actively cultivate ethical frameworks that prioritize transparency and accountability. Such commitment builds trust with customers, regulators, and the broader community.

Fostering a Leadership Pipeline in Indian Banks

22. It is an established fact that there exists leadership crisis at many levels of organizational management in Indian banks. The challenges for public sector and private sector banks are different in the space of the leadership pipeline but there is no debate about of existence of the challenges. In the case of PSBs, as the age profile of new leadership sees younger leaders, the transformation from a managerial position to a leadership position at times go through teething pains. The position of private sector banks is not very different as long serving leadership brigade hang their gloves. The regulatory intervention by way of October 2023 circular by RBI mandating at least two whole time directors in every private sector bank is a pointer to the uneven flow in the leadership pipeline. Further, the trend of exiting leadership sticking around in some other avatars around the bank also indicate their perceived indispensability or past domination, which is not a sound reflection of the pipeline. Leaders in large banks earn their peers' respect with their strategic and technical skills that further contributes to their capacity to lead with credibility. However, when executives get promoted to leadership positions merely because of technical competency and not personability, lack experience in contextualising, formulating strategy, setting goals, and making decisions due to a lack of strong interpersonal and analytical skills become all too apparent in leading a bank.

23. Adaptation of one-size-fits-all approach in leadership development programs, assuming common leadership and skill traits regardless of context and circumstances may also need a changed view. Some of the Indian banks continue to be at the cutting edge when it comes to developing leaders. They differentiate themselves by not having a handful of charismatic leaders. They work towards building a pipeline of leaders across the institution. These banks do not depend on informal ways of development, but rather execute on robust processes for leadership development. The Top banks do not focus on carrying out one-size-fits-all training programs but focus on creating a personalized and holistic leadership development process. Building a leadership pipeline is a scientific process and its core ingredients are (i) branding leadership by building an external reputation; (ii) getting leadership-mix right, closely tied to the business strategy; (iii) raising the bar for assessment, a moving target adapting continually to business realities; and (iv) continuous investment in development.

Conclusion

24. Banks and banking services remain essential to economies, despite repeat predictions of their imminent demise by tech pundits. To stay relevant, however, bank leadership need to adjust their business models and adapt to the new realities. The traditional role of banks is being increasingly challenged and maintaining the *status quo* is not a safe strategy for any bank. To the question as to when the challenges of leadership in bank is most obvious, an obvious and correct answer to this question is "all the time," though certain times are more likely than others. Leadership is usually the most difficult when the situation is changing or unstable, even far below VUCA situations. No matter what or how much is on the corporate agenda, leaders can't take their eyes off the fundamentals of the business, its strategy and risks. Leadership is a quality that is often attributed to individuals who possess a unique blend of vision, integrity, and the ability to inspire others. Such leadership qualities have not only contribute to the success of one bank but also sets a benchmark for leaders across industries. The leaders must have actionable vision; assess the institutional capabilities realistically and exploit as well as explore those. The leaders need to be more than just sponsor strategies or initiatives – they need to get behind the wheel and drive it. At the same time, successful leadership is more complex that one individual and often suffers from attribution error such as conflation of business success with leadership attributes. The leadership would look different depending on when it is assessed. So, good leaders are not creation of any formulaic potion.

I will end my remarks with one message to the participating leaders to pursue what Indira Nooyi called 'performance with a purpose.' I wish this unique program initiative of CAFRAL good success.

Thank You.

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[i] Banca Monte dei Paschi di Siena in Italy
[ii] The Madras Bank (later merged for The Bank of Madras) – one of the tributaries of present day SBI.
[iii] Kouzes J, Posner B (2003)The Leadership Challenge. Jossey-Bass,
[iv] Handbook of Statistics on Indian Economy (2022-23), Table 12,1,45
[v] AMFI Monthly Reports
[vi] Gartner Research: Hype Cycle for Emerging Technologies, 2023