**Human Capital in Transformed Financial Services – A Side View**[1]

Smt. Indrani Banerjee, Additional Director CAFRAL and distinguished participants of the conference. It is my privilege to be interfacing with CHROs and CLOs of the banks, chance of which is relatively not -so-frequent during routine regulatory processes.

It was a bit tricky idea to caption the address as 'human capital', rather than 'human resources' when the audiences are Chief Human Resource Officers. The first thought that crosses one's mind is that capital is the first item on liability side of the balance sheet. I am sure, we have reached an evolved state in 2023, where HR function in banks / NBFCs is not seen merely as a cost-centre. Second, capital is characterized by its long-term standing and risk absorbency, but the current run rate of employee turnover could take 'human resources' closer to physical resources with a clear trend towards a sharing and in-motion economy. Financial service has always essentially been a peoples business and as you know: businesses do not create value - people do. If one has to explain the part about 'transformed' in the title, it may be much extended than the catch phrase of 'digital transformation' producing weapons of mass disruption. There are increasingly more financial services that are being distributed by non-financial entitles. The employee cross-migration across different categories of financial service providers as well as that between financial and non-financial entities is rather mainstream these days. As a regulator, RBI relates to a very tangential cross section of HR but witnesses its distinctive effects on other spaces which it closely observes. Learning and Development is one arm of HR preparing the resources while the other arm manages such resources for effective running of the business.

**2.** The Great Resignation that played out in the west in early 2021 did not enact the same playbook in India. Nonetheless, its spill-over impact in India is reported to be manifesting in terms of steep rise in attrition and concomitant pay rise as the volatility persists, both variables reigning in double digits. On its top, issues like moonlighting too becomes another matter-at-hand signal of cautious eyeing at a gig economy. That is followed now by daily headlines about chunky lay-offs in certain frontier industries. The CHROs present in the room may perhaps be feeling relieved that the name of financial service industry does not feature so much in such stories. But that may at

[1] **Keynote Address by Jayant Kumar Dash, Executive Director, Reserve Bank of India at CAFRAL Conference of CHROs and CLOs on January 24, 2023 in Mumbai**

times be a misplaced in view of (i) increasingly blurring line between financial and non-financial sector employee catchment and (ii) receding role of staff cost - considered a controllable cost, as share of outsourced functions are on the rise. Given an oligopolistic market for supply of critical banking / financial technology, the ultimate pay volatility in those market may have to be borne by financial service providers. In other words, the imbalance between controllable and uncontrollable operating costs may tilt against the banks / NBFCs significantly dependent upon outsourcing book. The fact of banks/ NBFCs being highly regulated, again, stacks against them while increasingly dealing with employees of unregulated commercial entities without much competition. Entry of new players in the regulated spaces too add to the competition.

**Strategic Role for CHROs**

**3.**In the above backdrop, it would be contextual to raise the age-old topic of strategic partnership of a CHRO with CEO of a bank / NBFC versus playing a supporting role by delivering on administrative tasks. At the cost of repetition of what you might have learnt of Dr. Ram Charan in management classes, this requires redefining of CHRO's role such that the CXOs of financial capital and human capital join the CEO to form a triumvirate, what he called as G3 (Group of three). In redefined role, the CHRO, beyond handling usual HR responsibilities, has to carry out certain other critical activities. Three of such critical activities were identified as "*predicting outcomes, diagnosing problems and prescribing action on the people side that will add value to business. Some of these may seem like a usual charter for a CHRO, but they are largely missing in practice, to the disappointment of most CEOs*". Seven years after this view was authored, I am not sure to if this has lost its contemporariness. HR challenges are getting more complex by the day owing to fast evolving external and internal factors. In the challenging economy, the under-tapped potential of HR services in some of the good banks in India are apparent due to inadequate planning and slow response. The old saying 'if you fail to plan, you plan to fail' holds very invisibly true for HR adding to the complexity. HR Benchmarking is a toolkit in the hands of CHRO to measure performance against strategic priorities, future needs as well as peer group. It will indeed be a brave CHRO who can take the ownership of an agile business transformation in lockstep with business leaders of the bank / NBFC. Incidentally, Gartner research on CHROs Vision for 2023, though not specific to financial service industry, identified the top three priorities of CHROs as (i) leader and manager effectiveness (ii) organisational design and change management and (iii) employee experience.

**4.** Speaking of strategic HR, it would be interesting to look at some headline reported numbers of five largest public (PSBs) and private sector banks (PVBs) each, to notice the contrasts and convergences in efficiency and productivity metrics for first half of FY 2023, The average assets per employee for PVBs ranged between ₹6.70 – ₹14.10 crore as against ₹13.10 – ₹21.50 crore in PSBs. The cost incurred per employee for top five PVBs ranged between ₹3.90 to ₹5.40 lakh and that for PSBs was between ₹5.50 to ₹10.30 lakh. During the same period, the income generated per employee were in the rage of ₹19.60 – ₹36.80 lakh and ₹20.20 – ₹30.10 lakh respectively. Staff cost as a percentage of non-interest income for top PVBs was in the range of 25.60 – 38.90 per cent as against 54.20 – 61.00 per cent for PSBs. Income generated per employee (net of staff cost) was ₹15.70 – ₹32.70 lakh for PVBs as against ₹9.90 – ₹21.80 lakh for PSBs. While comparing between all pubic and top private sector banks, the top five banks in efficiency ratio and per-employee income generation consisted of 2 public and 3 private sector banks and top banks generating best per-employee net income consisted of 1 public and 4 private sector banks. However, five banks with lowest per-employee staff cost as well as staff cost to non-interest income ratio were all private sector banks.

**5.** During FY 2022, the highest remuneration to a whole-time director as a multiple of median employee remuneration ranged between 80x-170x for private banks. The percentage increase in median remuneration for employees of private sector banks ranged between 1.21 to 15.67 per cent. While such averages or ranges may not reveal any specific inference, juxtaposition of bank-specific details would reveal varying approaches to strategy relating to insourcing vs. outsourcing, skewedness of remuneration along different levels of employees and management and correlation with attrition rates.

Now I will outline a few of the HR linked aspects that regulators have generally traction with.

**HR Functions in Banks / NBFCs and Culture**

**6.** The Banking and NBFC Industry has emerged today as the main vehicle for the socioeconomic development of the country. It is often assumed that being a CHRO in a bank or other regulated financial entity is no different from being one in another service or manufacturing industry. Students of economics in their basic lessons learn that there are four factors of production: viz. land, labour, capital, and entrepreneurship for any business enterprise to run. For a financial service industry to run, without diminishing the relevance of land, capital, and entrepreneurship, the preponderance of the factor labor in unmistakable. That places the HR function in banks notches above similar functions in other industries. Further, given the 'special' nature of banks, the CHROs and CLOs carry an additional responsibility of high awareness about compliance at each step and the potential effect of inadequate HR / Learning policy or approach on the institution as well as the wider financial system. In fact, HR professionals in banks / NBFCs are likely to face more curveballs when it came to compliance issues due to fast-changing rules and new regulations in times to come. There have been numerous examples internationally as well as in India, some of them well publicized and some not so, where the slacks in human resource policy and approach, including the vigil and ethical work culture, has been instrumental in bringing disrepute and loss to the whole industry in addition to negative organizational outcomes.

**7.** Though culture is acknowledged to be the most crucial environment for employee motivation, engagement, and performance, the nature of the relationship between culture and the HR mechanisms for instilling the desired values in employee conduct needs better understanding. A study[2] found evidence that governance practices and financial incentives can reinforce culture. At the same time, incentives can work in counter direction to acceptable culture, particularly when employees are rewarded for achieving a business metric without regard to the actions taken to achieve that metric. It has been rightly quoted that people invariably will do what you pay them to do even when you're saying something different. The study found that over half of senior executives surveyed believe that corporate culture is among top-three drivers of firm

[2] Corporate Culture, evidence from the field by Graham, Harvey, Popadak, Rajgopal, NBER, March 2017

value and 92% believe that improving their culture would increase their firm's value. Executives link culture to ethical choices (compliance, short-termism), innovation (creativity, taking appropriate risk), and value creation (productivity, acquisition premia). These links have to be assessed within a framework for cultural effectiveness as a function of interactions between cultural values, norms, and formal institutions. Cultural norms are as important as stated values in achieving success.

**Employee / Executive Hiring**

**8.** The skill gaps in financial service industry is said to be continuously stretching and the traditional recruitment methods are slowly losing effectiveness. This in large part owe it to constantly increasing capability of digital technology. Emergence of new roles, some emanating from the technological developments and some from regulatory requirements, add to the demand-supply gap. The skills gap may be expected to widen in 2023-24 as the demand for skilled and experienced personnel continues to outpace the supply. Challenge for CHROs to identify / visualize the skill gaps and find creative ways to attract and retain talent is in the open for a long time. The banks and large NBFCs have been adapting to newer methods and channels to hire and onboard new employees at the base or customer-facing level from an extended talent pool. The hiring infrastructure of many such institutions has undergone changes. There have been significant trends observed in lateral hiring as well, even among PSBs, and the demand for mid-career bankers far outstrip its supply. While outsourcing of human resources from external entities, within the Group or otherwise, had been an option for private banks for long, there is a trend among some PSBs to have captive or collective entities to execute different types of functions / activities. Upskilling could be one of the options for banks/ NBFCs where it should mean reducing manual tasks and using technology to automate more processes. However, swiping technology talent from IT companies would be a delicate proposition as it may not be easy to migrate intellectually from a creative and entrepreneurial environment to a hierarchical one with bounded opportunity to work on interesting projects or learn. Frequent supervisory commentary underpins the deficient cultural fitness of many such external employees in customer and regulation focused contexts.

**9.** Talking of upskilling, it may be apt to mention about experience of certain Indian banks with necessary scale who have adopted Robotic Process Automation (RPA) for hundreds of business processes in order to depend less on human resources for repetitive manual back-office works cutting across varied functional areas. About most processes outside the core banking system could be a potential candidate of automation, altering performance & efficiency level and reducing recruitment / staffing issues for tedious activities. However, while replacing human resources with technology resources, the options would be highly dependent on factors such as technical feasibility, scale, effect on customer experiences and scope for risk mitigation.

**Compensation of Employee and Management**

**10.** India is one of the few banking jurisdictions where remuneration of MD & CEO / Whole Time Directors of private banks statutorily requires prior approval of the regulator. This may theoretically appear as a little bit of CHRO function handed over to the regulator. This often attracts two polar views from CHROs of foreign banks and that from fellow overseas regulators. Compensation of bank executives has been globally a hot topic through the business cycles and currently is. Broadly, RBI follows the principles of compensation guidelines of Financial Stability Board (FSB) while standing firmly on the foundation of provisions of the Banking Regulation Act. RBI has issued guidelines on compensation for Whole Time Directors (WTDs), all Material Risk Takers (MRTs) for banks. On the path to proportionate regulatory convergence, RBI has also issued guidelines on compensation to NBFCs, essentially on the elements.

**11.** It is well appreciated that compensation is very vital for attracting right fit talents to banking and other financial service entities. There is no doubt that it is a market determined variable. It may be difficult and not desirable to give a formulaic framework by regulator for remuneration for senior management of different banks, unlike CHROs who may be within their remit to do so. Nonetheless, there are elements in this ecosystem who tend to create some artificialities to the determinants. All that regulator does is to test the proposed numbers to ensure that it is right quadrant of the peers based on its size and performance; that it is risk-adjusted and non-volatile and in keeping with internal and external equity. However, some of the NRCs (CHROs) do appear in minor misalignment while balancing - heavy on what’s and light on how’s. Often, such views are aided by benchmarking exercise by external agencies whose models potentially tend to support certain kinds of biases. It has to be appreciated that in a market-based determination of compensation, an exceptional bump here and there can take the mark-to-market level artificially up across the board. This approach also spills over to executives down the hierarchy creating the wage spiral. That said, I must mention that there are a good number of NRCs and CHROs they are cognizant of a balanced approach and act as linchpins for the whole industry.

**Mobility and Talent Retention**

**12.** Latest research by Linkedin, a professional networking platform, in November – December 2022 has put 88 per cent employees in sub-24 age group and 64 per cent in 45-54 group are on the wings to switch jobs in India. While the trend for banks and other financial service institutions may relatively be lower but observed to be directionally similar. As per last year's estimate the attrition at lower levels in banks was in 30-50 per cent range and overall around 20 percent. As per the research, most mobility aspirants depend upon right networking, re-aligning with emerging business priorities and learning new in-demand skills to make the move. This can be both good and bad news for CHROs. Many a times, it is observed that a middle or top-level successful management personnel leaving a private financial service institution is not a stand-alone event when she leaves 'flock, stock and paddle' i.e leaving with the team and the strategic knowledge.

**13.** To be realistic in trend spotting, younger employees are likely to believe to be working for more rational reasons like pay rather than a sense of purpose or social connection. In an age of acceleration, the half-life of skills is continuously on a wane and managing a multi-generational workforce needs better empathetic skills. The percentage of millennials who favour working long term in financial service is said to be in teens. Fulfilling the material aspects of job is highly vulnerable to competition and hence attrition, creating a spiral. Banks and NBFCs who recognize the importance of balancing the tangible offerings with more long-term intangibles like growth opportunities, a tapestry of job options, connection, cultural developments and above all some meaning and purpose of pursuing the profession have instances of higher level of employee retention. This theory can be seen in action when one compares how certain banks continue to be the major talent pool and leader suppliers for many entities in the wider financial service sector.

**14.** A high value on attracting and retaining top talent must be placed. If the employees are well taken care of, the clients are well taken care of. Further, the cost of hiring such employees, their training and severance cost prove to be sunk cost and the cycle continues adding to the staff cost. There may be a need to create more upward mobility within the financial institution, which would reduce recruiting and onboarding costs. One of the most notable emerging trends in banking is a shift of HR from a project mindset to a product mindset meaning a shift from discreet pieces of activities to ongoing activities improving delivery quality and enabling building of capabilities. The shift is manifest in delivering value instead of following a plan or creating efficiency and changing the focus to customer from a solution. This is facilitated by evidence based HR is practices i.e making decision supported by evidence from available internal data, research findings and empirical studies, expert judgement and real experiences, values and concerns.

**Succession Planning**

**15.** One critical observation for many of the banks during last supervisory cycle was deficient or non-existent succession planning in banks and NBFCs. While the observations were majorly meant in respect of top executive positions, it has to be seen across all key positions in the context of (i) short term succession (ii) long term succession and (iii) management succession, each requiring a different set of key considerations. Proactive and competent succession planning and management is a key governance tool in promoting a bank's resilience and strategy. Succession management by HR function should reflect a dynamic planned distribution of roles, responsibilities, and cross-training for a management team to always have some "bench strength" . At smaller banks, the depth of talent readily available in-house for key management positions is typically limited. In contrast, larger banks usually have a deeper talent pool to consider for successors.

**Future Talent Requirements**

**16.** The current talent requirement has seen shifts from basic cognitive skills to socio-emotional and technological skills. The industry narratives put skills such as administrative and relationship management as oversubscribed. The profit optimization mindset, through cost excellence or otherwise, is in a kind of state of equilibrium. The gaps are seen in socio-emotional skills such as customer experience, communication, collaboration. Gaps in technological skills such as data science, robotics/AI are unmissable. Demands for talents in the areas of cyber security, big data engineer, app developers, customer journey or product design, customer experience continue to sustain and pose challenges for CLOs to keep the pipeline active. Banks and NBFCs have to analyse where they have long term gaps and develop a plan to narrow down or close these.

**17.** The banks / NBFCs may have to adopt an equivalent of pareto principle, say, a 'talent to value' approach which identifies the 'critical few' that drive, say, 80 per cent of business value. This has to be based on a solid data foundation rather than in a traditional hierarchical approach. Financial institutions tend to miss, say, 90 per cent of such critical talents when over-focused at the top. Once roles are identified, best performers need to be matched, developed and retained. On a lighter note, it will be interesting to know if any CHRO or CLO is counted among the 'critical few' in any bank or NBFC.

**18.** As we are pushing Banking 4.0, the design of human capital management too needs corresponding upgrade and reconstruction. Banking and other financial service evolve with its customers. Apart from the ubiquitous digitalisation, demographic trends, customer expectations and regulatory shifts, practical aspects of HR management and employee competency too should undergo transformation. The results of an European study[3] show that human resource management practices such as reskilling, upskilling, and redeployment are a solution to mitigate challenges in the Banking 4.0 era. An effectual design of a HRM roadmap for banks / NBFCs can ensure effective talent and workforce management. The CHROs and CLOs would have to construct the path with their information-driven imagination.

**Learning and Development Functions**

**19.** The L&D functions get their broad remit from the corporate strategy of revenue growth and improvement of productivity. A strategic L&D function generally

[3] Kuchciak, Iwa, and Izabela Warwas. 2021. Designing a Roadmap for Human Resource Management in the Banking 4.0. Journal of Risk and Financial Management

approaches it through development focus, competency based learning. However, the common lags observed in financial service L&D programs are in the areas of uninternalized core value, leadership and service mindset. Hence there may be a strong case of reconstructing learning culture and actively managing learning activity by creating a scalable learning infrastructure.

**Conclusion: Employee First**

Everybody would agree that banking evolves with customers. I am sure, every CHROs present in the room would have read Vineet Nayar’s book which has the following to say, I quote:

*“ The conventional wisdom says that companies must always put the customer first. In any services business, however, the true value is created in the interface between the employee and the customer. So, by putting employees first, you can bring about fundamental change in the way a company creates and delivers unique value for its customers and differentiates itself from its competitors*.”

It may be risky to draw a algebraic conclusion. However, from all the readings I have done, for an institution like a bank or NBFC, the consensus order of priorities could be (i) Employee (ii) Customers and (iii) Profit to have a sustained growth trajectory.

I will conclude here. I choose to give a miss to mention issues such as hybrid works, wellness and mental health, DEI (Diversity, Equity and Inclusion) etc. and a number of HR sub systems that are high points of contemporary HR conversation and important aspects for CHROs. However, regulators cannot stand in for HR professionals. With the conference day filled with a curated mix of speakers associated with HR advisory service and practice, I wish a very professionally stimulating experience to all the participants for rest of the day.

Thank you.

******