

# Banks modifying business models

Universal banks have become 'too big to handle' on account of regulatory challenges

**DOHA DATELINE**  
Dr R. Seetharaman

UNIVERSAL BANKS ARE diversified and provide liquidity to the financial markets and hence contribute to financial stability. They also provide financial services in a cost-effective manner through a single source.

Diversification of business activities not only serve as a better protector of a universal bank against external shocks that impact individual lines of business. But it also increases the likelihood of intra-firm contagion on account of external factors.

Universality as such does not complicate the lender-of-last-resort role of central banks. However, problems may arise when universal banks are typically large. If large institutions run into solvency problems, central banks may be confronted with the dilemma of "too big to fail". The "too big to fail" dilemma is related to their size and not related to the universality.

Universal banks not only enjoy benefits of large scale operations but also face complex regulatory challenges. Universal banks face enormous regulatory challenges in recent times. Some Universal banks had to pay penalties and fines for lapses in oversight and controls, deficiencies in risk management, non-compliance with money laundering issues and violation of sanctions. Universal banks have become "too big to handle" on account of the regulatory challenges.

The global regulatory reforms and the transformation in global financial architecture after the crisis impacted Universal Banking Groups. The Dodd-Frank Act in US came into law in 2010 and the Volcker rule placed restrictions on proprietary trading. Rules on transparency and centralised clearing for over-the-counter trading markets were introduced. The regulatory reforms under the Dodd-Frank Act had kept proprietary trading and

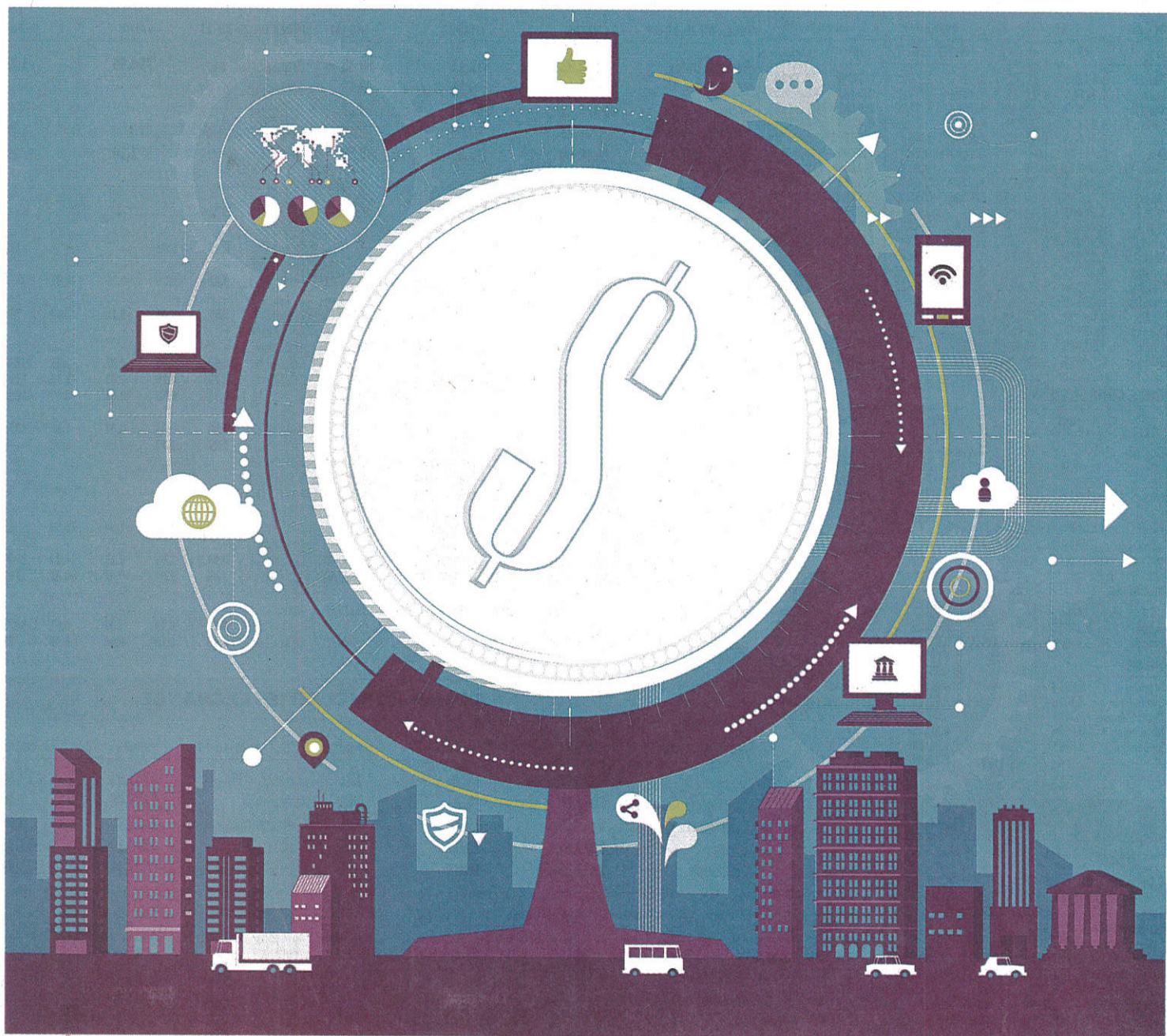
significant hedge fund investing outside the group and moved derivatives activities to affiliates.

The Vickers's commission in UK came with the recommendation of ring-fencing of UK banks' retail banking operations from higher-risk investment banking activities. The Volcker rule and the Retailing fence are designed to face the problem that arises from the integrated business models of financial institutions. In the Volcker rule it will still be challenging to separate market making and underwriting proprietary trading when assessing banks' exposures to securities markets. Similar challenges can also be faced in ring-fencing.

Basel III set consistent standards for capital and liquidity — which is critical in times of market stress. Basel III also provided a consistent 'level playing field' for banks around the world — that's essential in a globally interconnected system. Universal Banking is efficient but should develop safeguards as part of its current structural reforms. The structure of universal banks should be clear so that it would simplify the governance of banks and improve risk management. The responsibility and independence of the management is enhanced if business lines are separated to legal entities.

Universal banks which operate both retail deposit-taking business and wholesale global markets trading under the same roof are looking at ways to modify their business models to improve the return on capital. Universal banks are taking a capital-centric look at their business model and questioning which activities will be profitable. Balance sheet is scarce mainly in OTC (Over the Counter) products. There is a strategic rethink among universal banks about where best to deploy scarce capital for the benefit of their clients and shareholders.

Universal banks have abandoned business and locations, through



forced disposals or severe cost-cutting. Some of the universal banks have extended their corporate lending activities and maintained their retail networks, while modifying their capital markets operations to optimise balance-sheet consumption. The large universal banks

which dominate the most liquid markets benefit from the reduced risk appetite and trading activities of smaller players. They are also revisiting their strategies in business lines such as equity derivatives and fixed income. Some of them focused on asset management while

others exited or rebalanced the equity business. The destruction of shareholder value after the crisis has eclipsed the benefits of financial supermarket. There is indication of reduced wholesale trading activity, particularly in fixed income, currencies and commodities. This will

continue to emerge as regulation is phased in and shareholders increase scrutiny around capital usage.

*The writer is a group chief executive officer at Doha Bank. Views expressed by him are his own and do not reflect the newspaper's policy*

## An uptick in money laundering?

**ANALYSIS**  
M. Aftab

IS THERE AN UPTICK in the international money laundering? Anti-money laundering campaigners are, once again, having sleepless nights over it, and are raising their heads to counter it. They are forcing nearly a dozen key countries to do so.

Pakistan, at the centre of international terrorism, and itself its chief target is plagued by allegations of money laundering that feeds all the groups in the war-torn Afghanistan and the region. India, reportedly, among other countries, is one of the beneficiaries of such inflows.

Officials in the Ministry of Finance (MoF), and in multilateral institutions, including the International Monetary Fund, report "11



The Pakistani rupee will remain under strain, compared to the greenback and other hard currencies. — Bloomberg

When international gold prices declined in August-September this year, a huge amount of dollars was invested in duty free gold imports

ress on commitment to an action plan to address deficiencies related to anti-money laundering (AML) and combating financing of terror

preciation of the Pak rupee against the greenback during the last four months. It is also partly attributed to the rising value of the real estate in Dubai and the UAE, where some rich Pakistani families are buying property and others are making their dollar and investment safe as economic uncertainties continue to persist within the country.

But, with Pak rupee remaining under strain, compared to the greenback and other hard currencies, and a high rate of import duties on a wide range of products from food to consumer durables, smuggling-in will go on rising. It will continue directly to affect the value of the rupee downwards, and raise that of the dollar. That will happen with periods of comparative stability in the value of the rupee. Besides war-and defense-related equipment is also being smuggled in.

**NRI PROBLEMS**  
H. P. Ranina

**I am planning to return to India. I want to set up a small business. If I incorporate a company, would it entail procedural hassles?**

**P. K. Ranjan, Abu Dhabi**

Under the new Companies Act 2013, a small company can be incorporated which has certain advantages. A small company is defined to mean one having paid-up share capital of not more than Rs5 million or turnover not exceeding Rs20 million. One of the advantages is that small companies will not be required to hold four board meetings in a calendar year which is mandatory for other companies. They may hold only two meetings, one in each half of a calendar year.

In case of merger of two small companies, no approval of the National Company

the Investor Grievance Redressal Committee of the stock exchange which can award a monetary compensation. The stock exchange will block this amount from the broker's deposit and the broker will have seven days to decide whether to go to arbitration.

If the investor wins in the arbitration, and the broker moves the appellate body, fifty percent of the arbitration award or Rs150,000, whichever is less, would be given to the investor from the Investor Protection Fund. If the appellate order is in favour of the investor, he would get seventy five per cent of the money awarded subject to a limit of Rs200,000 minus the amount already given to him. The broker has the option to move the Court against the award of the appellate authority.

**My father-in-law who is resident in India has recently remitted through his bank**