

EARLY IMPRESSIONS

IMF's ECL Push: India's Balancing Act Between Growth and Stability



FOREWORD

The Indian banking sector is at a pivotal juncture as the Reserve Bank of India (RBI) carefully considers the implementation of the Expected Credit Loss (ECL) framework. While the International Monetary Fund (IMF) advocates for the immediate adoption of international standards such as IFRS 9, the RBI continues to take a measured approach, seeking to balance regulatory prudence with the need to support economic growth.

This note explores the differing perspectives by assessing both the immediate impacts and long-term implications for banking institutions and the broader financial system. The future trajectory of India's banking landscape will largely depend on how effectively the country navigates and balances its regulatory approach during this critical period of transformation.

We hope you find this analysis insightful and welcome the opportunity to discuss any specific aspects in further detail.



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NAVIGATING THE ECL TRANSITION:

A Strategic Roadmap for Indian Banks Amid Evolving Regulatory Paradigms

The Reserve Bank of India (RBI) has been actively implementing new guidelines to make certain that the Indian banking industry continues to be resilient and competitive on the global stage while also being robust financially. In January 2023, RBI published a discussion paper that signaled a move to a new ECL (Expected Credit Loss) framework for provisioning which indicated a significant change in risk management strategies. However, recently, the RBI has seemed to have adopted an accommodative stance around proposed regulatory changes, including the ECL framework for provisioning by banks. This measured approach underscores the RBI's balancing act between stability and growth, recognizing that regulatory reforms involve trade-offs. The central bank aims to strengthen the banking system without stifling credit growth or economic efficiency.



STABILITY VS. GROWTH:

The Balance

The RBI's stance on ECL provisioning and adoption of IFRS 9 principles is indicative of a turning point for Indian banks.

The RBI indicated that while the proposed regulatory changes aim to strengthen the risk management framework in banks and ensure that the regulated entities are financially and operationally resilient, there is a cost to implementing these regulations, which needs to be weighed against achieving economic growth and efficiency.



KEY IMPACT OF ECL ON THE BANKING SECTOR

While most of the banks have done significant work in the last few years to develop the ECL models and strengthen the overall model risk management framework, however the final shift from the Incurred Loss Model to ECL-based provisioning will redefine risk management and financial reporting in Indian banking:

**Variability in provisioning**

Although the ECL standards apply uniformly across the industry, there are varied practices adopted by the banks while developing ECL models (modelling practices, inherent assumptions, data availability, overlays, etc.) that might result in different outcomes even for the similar loan portfolios. These varying approaches and practices underscore the importance of the need for robust governance, transparent disclosures, and effective oversight

**Higher Capital & Compliance Costs**

While provisioning for credit risk may impact profitability in the short-run, it is expected to bolster resilience in the long-run

**Data & Technology-Driven Risk Management**

There is a shift towards digitalization in risk assessment due to the need for sophisticated credit risk modeling, stress testing, and analytics

**Increased Earnings Volatility**

ECL provisions fluctuate with credit risk, leading to greater earnings volatility, especially during economic downturns.

LONG-TERM BENEFITS OF ECL IMPLEMENTATION

While the challenges are plenty, this framework is bound to change Indian banking for the better:

**Proactive Risk Identification**

Sudden financial distress is eliminated as deteriorating credit quality is detected early

**Enhanced Financial Stability**

Capital buffers are strengthened when provisioned, which increases resilience to economic shocks

**Greater Transparency & Investor Confidence**

Trust in financial disclosures is improved due to increased accuracy of IFRS 9 compliant reporting

**Improved Credit Decision-Making**

Forward-looking risk assessment enables better risk-based pricing and reduces bias in credit allocation

**Competitive Advantage for Early Adopters**

Banks investing in advanced risk models and analytics will gain a strategic edge in a tightening regulatory landscape

THE IFRS 9 MANDATE:

IMF's Global Benchmarking vs. RBI's Pragmatism

The IMF, in its latest Financial System Stability Assessment (FSSA) report published by RBI on March 25, 2025, acknowledged India's robust economic recovery and effective regulatory measures, especially in the Non-Banking Financial Companies (NBFCs) sector. Nevertheless, the IMF emphasized the need for quicker adoption of IFRS 9 (ECL) standards, citing:

- Cross-border comparability for foreign investors.
- Reduced arbitrage between Indian GAAP and global accounting standards.

Thus, a nuanced approach emerges: while the IMF is prompting for quick adoption of IFRS 9 to align with global standards, the RBI prefers a calibrated approach and phased implementation strategy balancing the stability and growth of the economy.

RBI's calibrated response demonstrates strategic sovereignty:

- Phasing aligns with domestic banks' readiness (e.g., PSBs vs. tech-forward private banks).
- Parallel reforms (e.g., PCA framework tweaks) ensure ECL synergizes with broader stability goals.

FINAL THOUGHTS:

A Defining Moment for Indian Banks

Given the range of factors at play, including varying levels of preparedness among banks, the broader economic context, the IMF's push for IFRS 9 adoption, and the RBI's calibrated stance, it will be important to observe how this transition evolves. The RBI's efforts to strike a balance between financial stability and operational efficiency are likely to play a pivotal role in shaping the future of India's banking landscape over the coming years



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