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# Challenges and Opportunities: Transaction Banking in India and China

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India and China have long been heralded as the powerhouses of Asia. Certainly, both countries look set to maintain strong growth rates despite ongoing challenges. Inflation and high interest rates, for example, remain a problem for India, but its gross domestic product (GDP) is still expected to grow by 7% throughout 2012.*

Looking at China, its projected GDP for 2012 may dip below 8% for the first time in 20 years**, but this slower growth rate is seen as more sustainable and reflects a greater focus by the country on domestic consumption.

However, it must be noted that neither country is immune to the turbulence affecting international markets. Europe is an important economic partner to China***, and the slowdown of European consumption has had a knock-on effect on China's exports. Although India is a largely domestic-led economy, making it less dependent on exports to the West, Chinese demand for its natural resources and agricultural products has waned.

This combination of domestic and international challenges means that corporates in both countries are chiefly concerned with keeping a tight grip on liquidity, optimising working capital efficiency and closely managing counterparty risk.

## Addressing Domestic Challenges

In view of the current environment, the spotlight is now firmly on transaction banking, a sector noted for its relation to the "real" economy. Both China and India are undergoing significant changes in this area.

In China, for example, the past decade has seen rapid progress in regulation and technology. While regulation had presented a barrier to development in the past, transaction banking products and services *are* evolving and are expected to come to market quickly as deregulation occurs. However, it must be noted that deregulation is a slow process hampered by regional regulatory bodies with varying legal frameworks.

Indeed, China's network of fragmented local clearing systems looks set to remain in place even as the country pushes for an upgraded national payments system. This elevated system, China's National Advanced Payment System (CNAPS) 2, offers broader functionality and allows large amounts of RMB to be cleared across regional borders. However, compliance will remain a complex issue because of domestic fragmentation.

Regulation and automation are also key issues in India, which has more than 1,000 clearing zones and 78,000 local and foreign bank branches. However, the rise to dominance of electronic payments has gone a long way to improving efficiency. That said, 55% of small value payments are still processed manually, which remains a treasury nightmare.

A further problem, one that is almost unique to the subcontinent, is the great variation in transaction types. They range from the smallest of vendors selling products in remote villages to multinational corporations (MNCs) handling huge domestic and cross-border transaction volumes. Partnerships between local and global banks are offering viable solutions to achieving geographical coverage, account consolidation and processing efficiency. When combined with advances in technology, these bank partnerships are helping to fuel sector progress.

## Improvements for Corporates

Yet the increasing sophistication of technology and growth of bank partnerships are not the only ways in which the operating environment is improving for Chinese and Indian corporates. In some cases, regulation is also helping.

Take working capital management as an example. Optimising working capital management is important for corporates in both China and India due to the gap between the lending rate and the deposit rate. In recognition of this, Shanghai and

Beijing have launched schemes allowing MNCs to establish regional treasury centres in China, which offer preferential policy treatment and streamlined approval processes.

While there are at present no such schemes in India, the cash management hurdles created by cash-pooling restrictions and cross-border cash-pooling prohibitions can be addressed by sophisticated, automated, foreign exchange payments solutions and import documentation management services.

## Moving Forward

Looking to the future, there is every reason — largely thanks to technology — to be optimistic about the development of transaction banking in China and India. In China, the upgrade to CNAPS 2 comes hand-in-hand with efforts to increase connectivity to the SWIFT global payment system. Once implemented, cross-border RMB payments will become easier. China is also seeing greater connectivity between the RMB clearing system and other capital markets systems, such as the stock exchange or the central clearing system for bonds.

In India, the Reserve Bank has set up the National Payments Corporation of India (NPCI) as an independent entity to build state-of-the-art, consumer-friendly electronic retail payments systems that would be available around the clock. Some of the key initiatives taken by NPCI, such as mobile payments through the Interbank Mobile Payment Service, would have significant improved efficiencies for corporates in India for domestic collections and payments.

Such technological advancements — when combined with the efforts of local and global banks to work together — can address corporates' current efficiency, liquidity and risk concerns, as well as address future market changes and challenges.

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