



Yes Bank crisis: A case study on lapses in anti-money laundering and risk management practices

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Abstract

This Case Study on The Yes Bank crisis is a powerful reminder of the consequences of rapid growth on corporate governance, legal systems, risk management and AML protocols. It's a perfect example of what can go wrong when things move too fast. Using an exploratory research design that is based only on secondary data collected from Yes Bank's annual reports, regulatory filings and other industry sources and the study reviews the financial performance of the bank in three phases: pre-crisis, crisis and post crisis. Non-performing asset ratios, capital adequacy, net interest margins and the cost to income ratios were analysed in order to identify the cause of the crisis to include loose lending standards, asset quality deterioration and weak AML/ KYC controls. The findings show that although regulatory interventions such as injection of capital and management change by the RBI brought back some stability, there are still a number of issues to be addressed in order to build the confidence of the stakeholders and to achieve financial stability. This paper therefore concludes that there is need to embrace growth with caution especially when it comes to risk management, governance and legal compliance and thus presents a reference model for other banking institutions and regulators especially in emerging markets.

Keywords: Asset quality, corporate governance, AML, KYC, non-performing assets (NPAs), capital adequacy, efficiency, and risk management

Introduction

Established in 2004, Yes Bank was one of the top private sector banks in India growing very fast and characterized by corporate lending and high growth rate. Under Rana Kapoor's leadership, Yes Bank took small steps in building its corporate lending segment and focused on sectors like real estate, Internet Banking, Mobile Technologies, Pharmaceuticals, Renewable energy, Electricals and Media (Ayush Kumar, 2021)^[6]. This led to a rapid growth but at the same time the bank was vulnerable to financial volatility as it had overexposed itself to risky clients.

But in the late 2010s, when Yes Bank found its NPAs had risen sharply, the problems highlighted serious financial issues, and poor risk management, bad governance, or even financial misconduct. The liquidity problem was such that the bank had been, in part, exposed to some distressed companies, including IL&FS, DHFL, Jet Airways and the Anil Ambani Group. Moreover, AML and KYC regulations were found to be weak and the bank was suspected of being used to hide suspicious transactions.

RBI intervened in March 2020 to restructure the powers of the bank. The RBI imposed a 30-day moratorium period and replaced the current administrator with Mr Prashant Kumar, who was previously serving as deputy managing director of the State Bank of India (SBI) (Business Standard, n.d.). In addition to this, the withdrawal limit of ₹50,000 was fixed per account during the moratorium period (Misra, 2020)^[9].

This case study aims to analyse the failure of Yes Bank and identify the essential gaps in governance, risk management and regulatory oversight. The paper will also investigate the long-term consequences of the crisis for India's banking system and will provide recommendations on how to strengthen regulatory frameworks, corporate governance and financial risk management practices to prevent such crises in the future.

Literature Review

Abraham Telar Nicknora (2024) studied examines the relationship between Anti-Money Laundering (AML) compliance, particularly focusing on customer due diligence, and the financial performance of selected commercial banks in South Sudan.

Ankita B. Jaiswal, Deepak S. Sharma (2024) wrote a Research Article on YES BANK scam: An overview on fraudulent practice and implications regulatory.

Bezawada Brahmaiah (2022) examines the market risk and liquidity risk management techniques and practices followed by the Indian scheduled commercial banks (SCBs), compare market and liquidity risk management practices between the PSBs and PVSBs and review the strategies adopted by the SCBs in market risk management practices.

Tushar Ranjan Barik (2022)^[7] studied the factors that led to the failure, consequently the bankruptcy events, and also the role of RBI in the survival of the Bank.

Shakeb Akhtar, Mahfooz Alam, Mohd Mohsin Khan (2021)^[8] presented case study based on the nation's biggest-ever banking failure of India's fastest-growing private bank, YES Bank. The YES Bank fiasco showcases the prevalent flaws of uprising NPAs and mounting bad debts in the financial sector.

Noura AI Suwaidi and Haitham Nobanee (2020) studied past research and the development of knowledge and practice in the area of countering money laundering and terrorist financing to draw attention to the gaps in the preventive mechanisms adopted by countries to fight against anti-money laundering (AML) and anti-terrorism financing (ATF).

Mohammad Sleimi (2020) studied effects of risk management practices on banks' performance: An empirical study of the Jordanian banks.

Bashir Muhammad, Sher Khan, Yunhong Xu (2018) examined how risk management practices can be influenced by factors, including understanding risk management, risk assessment & analysis, risk identification, risk monitoring and credit risk analysis in commercial banks.

Prabhakar, Dr. S. Mathivannan, J. Ashok kumar (2017) the asset liability of commercial banks' balance sheets presented significant difficulties since the banks directly affected their operations, profitability, and ability to compete. The nation's RBI concentrated and counselled banks to take decisive actions to reduce the asset-liability management mismatch.

Kumar, (2014), studied on research, the most important factor which banks required to manage now days is liquidity. This study analysed short term liquidity and maturity gap of the banks in order to decrease risk in banking sector. This survey help banks to reduce the risk which is very essential for all financial institution in India.

Dr. Anurag Singh, Priyanka Tandon (2012) One of the crucial instruments for risk management in Indian commercial banks is asset-liability management, or ALM. The Indian banking sector is vulnerable to a variety of market risks. The research paper talks about asset liability management problems.

Profile of YES Bank

Yes Bank is one of the largest private sector bank in India and was established in the year 2004 by Rana Kapoor and Ashok Kapur to cater to the Future Businesses of India (Yes Bank).

Business Operations: Mainly a corporate bank with retail banking and asset management operations. It has several main divisions in its operations:

- Corporate and Institutional Banking
- Commercial Banking
- Investment Banking
- Corporate Finance
- Financial Markets
- Retail Banking

Branch Network: As on June 30, 2019, YES Bank had a network of 1,122 branches and 1,220 ATMs in India. The bank has been aggressively expanding its network, adding 85 branches in the fiscal 2023-24 to reach a total of 1,234 branches. The bank has also planned to expand its branches with opening of over 100 branches by FY 2025-26. (fortuneindia.com)

Strategic Collaborations and Financial Measures: In terms of collaborations and finance, YES Bank has undertaken the following measures to enhance its service:

- **Syndicated Loans:** Yes bank had taken syndicate loans from eight large international entities including ADB, OPIC, European Investment Bank, bank in Tiwan and Japan for amounts ranging from US\$ 30 Million to US\$ 410 Million, which it in turn lends to small and medium scale enterprises as well as large corporate. It has also both taken as well as given short term loans to a number of retail and corporate banks in Taiwan, Japan, USA and Europe. (Dr. D.V. Ingle, 2018)^[13].

- **International Collaborations:** Yes Bank also has strategic partnerships with OPIC (United States World Bank) and Wells Fargo to further extend global reach.

Recent Developments: Yes Bank has developed a rural model in the last few years. During FY23 the bank added another 83 branches taking the total to 1,192, with 450 branches in semi-urban and rural areas. Additionally, YES Bank is planning to buy microfinance institutions (MFIs) to strengthen its footprint in emerging rural markets as well as increase its agriculture priority sector lending. (business-standard.com)

Need and Significance of the Study

In the banking sector, the Yes Bank crisis revealed severe deficiencies in risk management, anti-money laundering (AML) compliance and corporate governance in the banking sector. There is a dire need for this study in order to identify these systemic deficits and fill the knowledge and regulatory practice gaps. Learning from the root causes of the crisis, including lenient lending to low-quality borrowers, weak in-house checks, and slow-moving regulatory action, are also key to more-focused.

This study is significant because it may inform practice and policy. This study aims to make a meaningful contribution to the banking sector by providing practical recommendations for the enhancement of anti-money laundering (AML) practices, corporate governance, and risk management frameworks. The study will eventually protect the interest of investors and depositors, prevent future financial crises, and set a precedent for future investigations into financial stability in developing countries.

Objectives of the Study

1. To Analyse the Gaps in Yes Bank's Risk Management Framework
2. To Assess the Weaknesses in Anti-Money Laundering (AML) Practices at Yes Bank
3. To Recommend Strategies for Strengthening Risk Management and Anti-Money Laundering Practices in Indian Banks

Research Methodology

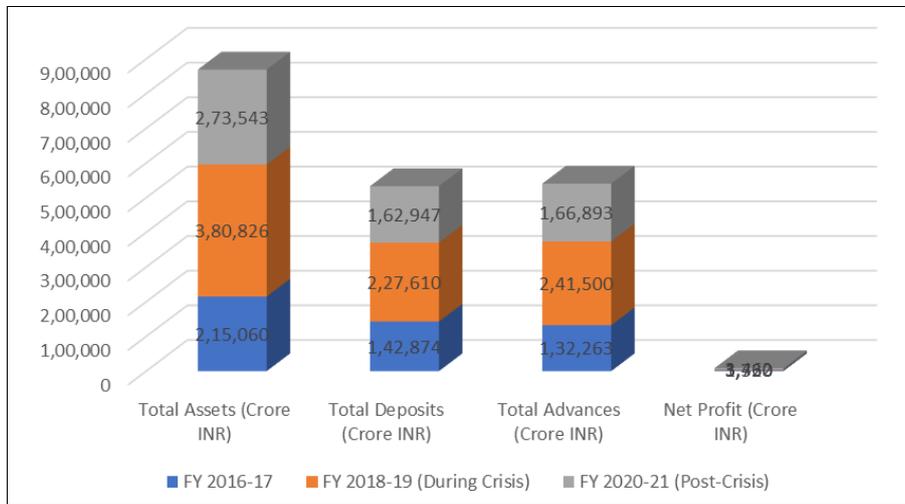
This study is based on the exploratory research design on secondary data from publicly available financial statements of Yes Bank. This analysis highlights the intervention between three key dates—Pre-Crisis, During Crisis, and Post Crisis—regarding three important financial aspects in the analysis of a bank—Total Assets, Total Deposits, Net Profit, and NPA Ratio. This methodology seeks to show trends and provide quantitative measures of the level of the impact of the crisis on the bank's financial health.

Data Analysis and Interpretation

The analysis of this study is done by taking secondary data from Yes Bank's annual reports, balance sheets, and published materials. The data represents three distinct periods: Pre-Crisis (FY 2016-2017), During Crisis (FY 2018-2019), and Post-Crisis (FY 2020-2021), covering the financial key indicators which depict the bank's performance as well as its risk profile during this time period.

Financial Performance Metrics of Yes Bank

Metric	FY 2016-17 (Pre-Crisis)	FY 2018-19 (During Crisis)	FY 2020-21 (Post-Crisis)
Total Assets (Crore INR)	2,15,060	3,80,826	2,73,543
Total Deposits (Crore INR)	1,42,874	2,27,610	1,62,947
Total Advances (Crore INR)	1,32,263	2,41,500	1,66,893
Net Profit (Crore INR)	3,330	1,720	3,462



(Source: The Authors)

Interpretation

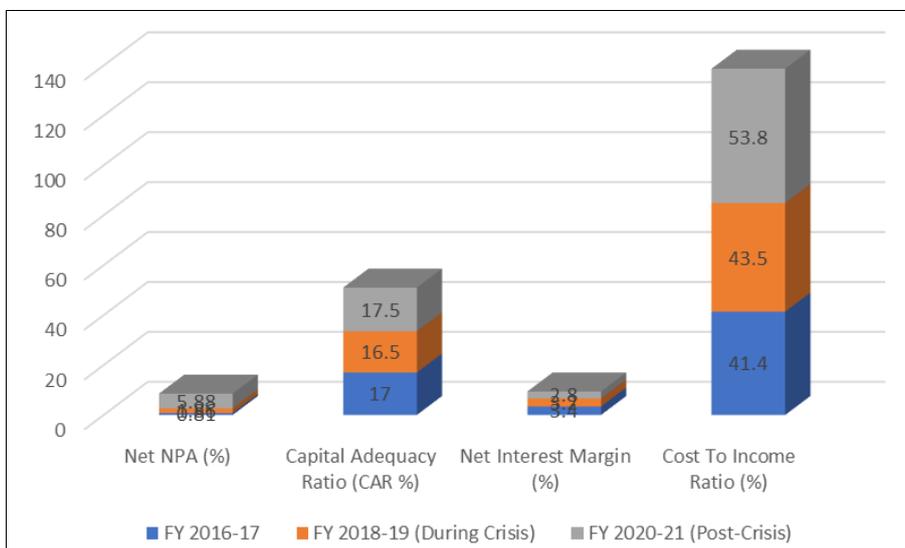
- **Total Assets & Deposits:** The major growth in assets (from 2,15,060 to 3,80,826 Crore) and deposits (from 1,42,874 to 2,27,610 Crore) during the crisis shows an aggressive strategy to expand. Yet, the later decrease after the crisis (assets down to 2,73,543 Crore and deposits to 1,62,947 Crore) points to efforts to reduce debt and bring stability.
- **Total Advances:** Advances grew by more than 100% during the crisis (from 1,32,263 to 2,41,500 Crore) suggesting quick and dangerous lending. The drop to

1,66,893 Crore after the crisis points to a pullback in lending as the bank tried to control risk.

- **Net Profit:** The bank's profitability also declined sharply in the crisis phase (from 3,330 Crore to 1,720 Crore), showing the negative effect of increasing NPAs and increased expense. Post-crisis increases in net profit (to 3,462 Crore) indicates partial return to operations though this can be negated with continuing asset quality concerns.

Key Risk and Efficiency Metrics of Yes Bank

Metric	FY 2016-17 (Pre-Crisis)	FY 2018-19 (During Crisis)	FY 2020-21 (Post-Crisis)
Net NPA (%)	0.81	1.86	5.88
Capital Adequacy Ratio (CAR %)	17.0	16.5	17.5
Net Interest Margin (%)	3.4	3.2	2.8
Cost to Income Ratio (%)	41.4	43.5	53.8



(Source: The Authors)

Interpretation

- **Net NPA (%):** The Net NPA ratio skyrocketed from 0.81% in FY 2016-2017 to 5.88% in FY 2020-2021 which resulted due to declining asset quality of Yes Bank. This increase shows the high proportion of Non-Performing loans as compared to other banks.
- **Capital Adequacy Ratio (CAR %):** The CAR was 17.0% before the crisis and it reduced to 16.5% during the crisis. After the crisis it increased to 17.5%. The bank's efforts in reducing and controlling its NPAs have been partially successful in as much as it has been able to get the capital back to pre-crisis levels, but the improvement in the ratio has not been felt.
- **Net Interest Margin (NIM %):** The NIM reduced from 3.4% pre-crisis to 2.8% post crisis. The decrease in NIM indicates that the profit that the bank makes from its main lending activity has decreased due to low interest income as opposed to high costs, say.
- **Cost-to-Income Ratio (%):** The Cost-to-Income ratio, in the immediate aftermath of the crisis, rose from 41.4% in the pre-crisis years to 53.8%. This is rather worrying as when compared to other ratios the bank's operational income has plummeted in relation to the operational costs which in turn shows that the bank has become more inefficient and has had to spend more in order to manage a larger risk weighted asset base.

Impact of the Crisis

The crisis at Yes Bank impacted multiple aspects of the banking sector — to depositors, investors, the operational framework of the bank, and the general regulatory landscape.

Depositors: The bank restricted withdrawals due to liquidity problems, causing service interruptions. So many customers have visited multiple ATMs but none of them dispensed money and some also tried using digital banking but was unable to transfer funds to their other bank accounts (Tushar, 2022). Depositors outright lost trust in the bank's ability to hold their money, leading to mass hysteria.

Investors: About 32 mutual fund schemes are exposed to Yes Bank debt with a total exposure of ₹2,848 crore. Many of these bonds are AT 1 (Additional Tier 1) bonds which are designed to absorb losses when the capital of the bank falls below a certain level (LiveMint.com). The steep fall in Yes Bank's share price in the wake of the crisis wiped out investor wealth. Bothered, by this fall, matters both pure risk management too life balance wheel: scale, and economic balance, or economic health.

Financial Health: The crisis caused an escalation in non-performing assets (NPAs) levels implying deteriorating asset quality. the bank's reported stressed assets stood at ₹100,000 million, owing to its exposure in infrastructure, real estate and entertainment sectors (Sinha, 2019) ^[10]. It reported a huge downfall in its profits, from ₹42,240 millions in 2017-2018 to ₹1,720 millions in 2018-2019 (Adhikari, 2019) ^[12], since it earned the title of 2019's world's worst lender (Ghosh, 2019) ^[11].

Banking Sector: Regulators boosted oversight and passed reforms intended to tighten risk management across the sector, in response to the crisis. It prompted an industrywide re-evaluation of lending standards and governance practices (Business Standard, 2020).

Economic Impact: The reduced lending by the bank resulted in even less credit available for critical industries including real estate and infrastructure. Both factored into a broader economic slowdown that also being felt in overall economic growth (Financial Express, 2019).

Role of RBI in Yes Bank's Reconstruction

- The Reserve Bank of India (RBI) placed in public domain a draft scheme for reconstruction of Yes Bank.
- State Bank of India has expressed its willingness to make investment in Yes Bank and participate in its reconstruction scheme. SBI can invest for up to 49 per cent stake for nearly Rs 2,450 crore.
- The central bank had invited suggestions and comments from members of public, including the banks' shareholders, depositors and creditors on the draft scheme. Suggestions will be received by RBI till Monday march.
- Earlier in the day, RBI governor Shaktikanta Das had assured depositors that resolution efforts were being taken to maintain "stability and resilience" in the financial sector and hurdles would be cleared "very swiftly".
- RBI placed Yes Bank under a moratorium late on Thursday, saying it was taking control of it for 30 days and would work on a revival plan. RBI also named Prashant Kumar, SBI's former chief financial officer, as Yes' administrator. The central bank also limited withdrawals.

(The Economic Times,2020)

Recommendations

- Install strong systems to identify risks in activities that are critical to the success. Make use of automation and advanced technology for better management and minimizing mistakes. Monitor transactions by using real-time analytic tools.
- Manage the loan portfolio effectively to spread the risk and limit the exposure to risky areas.
- Check the credit-worthiness of borrowers before provide loans to avoid bad debts and keep a keep on their financial health.
- Carefully select the auditors as they play a huge role in checking the legal compliance of activities undertaken.
- Establish an independent board of directors and special committees for risk management and better control.
- Regularly review and update AML and KYC protocols to comply with global standards.
- Regularly provide training to employees for better compliance of rules and regulations.
- Keep transparency by sharing information regularly with stakeholders.
- Set up a contingency plan to avoid the losses to depositors, investors and other stakeholders in case of crisis.

Conclusion

The Yes Bank crisis is a classic example of the consequences of risks that are associated with quick growth that threatens corporate governance, legal compliance, and societal norms. The growth strategies adopted by Yes Bank— increased exposure to high- risk loans, deteriorating asset quality, weak corporate governance and reduced operational efficiency resulted in its downfall. It also shows the deficiencies in AML and KYC practices of the bank.

The revival efforts by RBI led to its partial recovery, with improvements in risk management, corporate governance and AML practices. However, more needs to be done to earn back the full confidence of stakeholders which can be achieved by maintaining effective communication and transparency with stakeholders.

Moving forward, the lessons learned from the Yes Bank Crisis have helped in re-examination and development of bank's internal structure and regulatory frameworks. This case is an eye- opener for everyone and teaches us the importance of striking a balance between growth strategies with financial stability, risk management, and legal compliance.

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