Decline in the Financial Performance of Banking Sector – A Study

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Abstract

The Indian banking system consists of 20 public sector banks, 22 private sector banks, 44 foreign banks, 44 regional rural banks, 1,542 urban cooperative banks and 94,384 rural cooperative banks, in addition to cooperative credit institutions. As on March 31, 2017, the total number of ATMs in India increased to 2,21,703 and is further expected to increase to 407,000 by 2021. As of 2017, 80 per cent of the adult population has bank accounts. As on March 31, 2017 the number of debit and credit cards issued were 925 million and 47 million, respectively. As of Q3 FY19 (between April–September 2017) total credit extended by commercial banks surged to Rs 90.81 lakh crore (US$ 1,299.39 billion) and deposits grew to Rs 120 lakh crore (US$ 1,866.22 billion). Assets of public sector banks stood at Rs 108.82 crore (US$ 1,557.04 billion) in FY18. As per Union Budget 2017-2017, Provision coverage ratio of banks reached highest in 7 years. As per RBI, as of December 20, 2017, India recorded foreign exchange reserves of approximately US$ 454.94 billion.

Indian banks are increasingly focusing on adopting integrated approach to risk management. The NPAs (Non-Performing Assets) of commercial banks has recorded a recovery of Rs 400,000 crore (US$ 57.23 billion) in FY2017, which is highest in last four years. Banks have already embraced the international banking supervision accord of Basel II, and majority of the banks already meet capital requirements of Basel III, which has a deadline of March 31, 2017.As per Union Budget 2017-20, investment-driven growth requires access to low cost capital which an requires investments of Rs 20 lakh crore (US$ 286.16 billion) every year.Reserve Bank of India (RBI) has decided to set up Public Credit Registry (PCR) an extensive database of credit information which is accessible to all stakeholders. The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017 Bill has been passed and is expected to strengthen the banking sector. In June 2017, RBI sets average base rate of 9.18 per cent for non-banking financial companies and micro finance institutions borrowers for quarter beginning of July.

Rising incomes are expected to enhance the need for banking services in rural areas and therefore drive the growth of the sector. As of September 2017, Department of Financial Services (DFS), Ministry of Finance and National Informatics Centre (NIC) launched Jan Dhan Darshak as a part of financial inclusion initiative. It is a mobile app to help people locate financial services in India.

Key words: banking, loans, performance, credit, customer, corporate, India.

Introduction

Indian Banking Industry originated in the first decade of 18th century as The General Bank of India came into existence in the year 1786. And then later Bank of Hindustan was started. The India's oldest bank which is in existence is the State Bank of India being established as "The Bank of Bengal" in Calcutta in June in the year 1806. A couple of decades later in the year 1850 the foreign banks like Credit Lyonnais started their operations in Calcutta. Calcutta was the most active trading port at that time which was during the British Empire, due to these reasons the banking activity took roots there and prospered. In the year 1865, the first fully Indian owned bank was established in Allahabad.

Punjab National Bank was established expanding the markets by the 1900s, Bank of India the year in 1895 in Lahore and the same Bank of India 1906, in Mumbai - both were founded under private ownership. Then later in the year 1935, the Reserve Bank of India formally took over the responsibility of regulating Indian banking sector. In the year 1947, after India's independence the Reserve Bank was nationalized and given more powers.

The Indian Banking Industry in 1960 became an important tool to facilitate the financial development of the Indian economy. Simultaneously it emerged as a large employer and debate prevailed that ensured about the possibility of nationalization of the banking industry. The then Prime Minister of India, Indira Gandhi expressed the intention of the GOI in the annual conference of the All India Congress Meeting. This was received with positive enthusiasm by the whole nation. Later the GOI was issued an ordinance and nationalized the 14 largest commercial banks with effect from the midnight of July 19, 1969. In 1980 for the second time nationalisation of 6 more commercial banks was done. The nationalization was done to give the government more control of credit delivery. With this the GOI controlled around 91% of the banking business of India.

Narasimha Rao government formulated a policy of liberalization in the year 1990 and gave licenses to a small number of private banks, which was known as the New Generation tech-savvy banks, some of the banks were like the UTI Bank(now re-named as Axis Bank) ,ICICI Bank and HDFC Bank. Liberalization along with the rapid growth in the economy of India boosted the banking sector in India, which has seen strong contribution from all the three sectors of banks, namely, government banks, private banks and foreign banks. The next stage for the Indian Banking Industry was to setup with the proposed relaxation in the norms for Foreign Direct Investment, where voting rights were given to all the Foreign Investors in banks which could exceed the present cap of 10%, at present it has gone up to 49% with some restrictions.

Indian Banking Industry was completely shooked with the new policy. Till this time the Bankers used to the follow the 4-6-4 method (Borrow at 4%; Lend at 6%; Go home at 4) of functioning. This new wave ushered in a modern outlook and tech-savvy methods of working for traditional banks which led to the retail boom in India. People not only just demanded more from their banks but also received more. Today Banking in India is generally fair and mature in terms of supply, product range and reach though in rural India still remains a challenge for the private sector and foreign banks. Banking in terms of quality of assets and capital adequacy, banks in India are considered to have clean, strong and transparent balance sheets relative to other banks in comparable other economies. The Reserve Bank of India is the autonomous body, with has the minimal pressure from the government.

The Reserve Bank of India had permitted Warburg Pincus to increase its stake in Kotak Mahindra Bank (a private sector bank) to 10% in March 2006. It is the first time an investor has been allowed to hold more than 5% in a private sector ban. As the RBI announced norms in 2005 that any stake exceeding 5% in the private sector banks.

Objective:

This paper seeks to explore the declining mode of financial performance in banking sector and the reasons behind this trend

Role of RBI in Bank regulation

As per the Reserve Bank of India (RBI), India's banking sector is sufficiently capitalised and well-regulated. The financial and economic conditions in the country are far superior to any other country in the world. Credit, market and liquidity risk studies suggest that Indian banks are generally resilient and have withstood the global downturn well.

Indian banking industry has recently witnessed the roll out of innovative banking models like payments and small finance banks. RBI's new measures may go a long way in helping the restructuring of the domestic banking industry.

The digital payments system in India has evolved the most among 25 countries with India's Immediate Payment Service (IMPS) being the only system at level 5 in the Faster Payments Innovation Index (FPII)

The Indian banking system consists of 18 public sector banks, 22 private sector banks, 46 foreign banks, 53 regional rural banks, 1,542 urban cooperative banks and 94,384 rural cooperative banks as of September 2017. In FY07-18, total lending increased at a CAGR of 10.94 per cent and total deposits increased at a CAGR of 11.66 per cent. India's retail credit market is the fourth largest in the emerging countries. It increased to US$ 281 billion on December 2017 from US$ 181 billion on December 2014.

The digital payments revolution will trigger massive changes in the way credit is disbursed in India. Debit cards have radically replaced credit cards as the preferred payment mode in India, after demonetisation. Transactions through Unified Payments Interface (UPI) stood at 1.2 billion in November 2017 worth Rs 1.89 lakh crore (US$ 27.08 billion).

As per Union Budget 2017-20, the government has proposed fully automated GST refund module and an electronic invoice system that will eliminate the need for a separate e-way bill.

The total equity funding of microfinance sector grew at the rate of 42 year-on-year to Rs 14,206 crore (US$ 2.03 billion) in 2017-19.

Deposits under Pradhan Mantri Jan Dhan Yojana (PMJDY) stood at Rs 1.06 lakh crore (US$ 15.17 billion) with 37.34 crore accounts registered. In May 2017, the Government of India provided Rs 6 lakh crore (US$ 93.1 billion) loans to 120 million beneficiaries under Mudra scheme. As of November 2017, the total number of subscribers was 19 million under Atal Pension Yojna.

Key investments and developments in India's banking industry include:

In October 2017, the Department of Post launched the mobile banking facility for all post office savings account holders of the CBS (core banking solutions) post office.

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In October 2017, Government e-Marketplace (GeM) signed a Memorandum of Understanding (MoU) with Union Bank of India to facilitate a cashless, paperless and transparent payment system for an array of services.

Transactions through Unified Payments Interface (UPI) stood at 1.15 billion in October 2017 worth Rs 1.91 lakh crore (US$ 27.33 billion).

In August 2017, the government announced the major mergers of public sector banks which included United Bank of India and Oriental Bank of Commerce to be merged with Punjab National Bank, Allahabad Bank will be amalgamated with Indian Bank and Andhra Bank and Corporation Bank will be consolidated with Union Bank of India.

The NPAs (Non-Performing Assets) of commercial banks has recorded a recovery of Rs 400,000 crore (US$ 57.23 billion) in last four years including record recovery of Rs 156,746 crore (US$ 22.42 billion) in FY19.

The board of Allahabad bank approved the merger with Indian bank for the consolidation of 10 state-run banks into the large-scale lenders.

As of September 2017, the Government of India launched India Post Payments Bank (IPPB) and has opened branches across 650 districts to achieve the objective of financial inclusion.

The total value of mergers and acquisition during 2017 in NBFC diversified financial services and banking was US$ 2,564 billion, US$ 103 million and US$ 79 million respectively @.

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Government Initiatives

As per Union Budget 2017-20, the government has proposed fully automated GST refund module and an electronic invoice system that will eliminate the need for a separate e-way bill.

Under the Budget 2017-20, government has proposed Rs 70,000 crore (US$ 10.2 billion) to the public sector bank.

Government has smoothly carried out consolidation, reducing the number of Public Sector Banks by eight.

As of September 2017, the Government of India has made the Pradhan Mantri Jan Dhan Yojana (PMJDY) scheme an open ended scheme and has also added more incentives.

The Government of India is planning to inject Rs 42,000 crore (US$ 5.99 billion) in the public sector banks by March 2017 and will infuse the next tranche of recapitalisation by mid-December 2017.

Achievements

Following are the achievements of the government in the year 2017-18:

As on March 31, 2017 the number of debit and credit cards issued were 925 million and 47 million, respectively.

As per RBI, as of October 25, 2017, India recorded foreign exchange reserves of approximately US$ 442.58 billion.

India ranks among the top seventh economies with a GDP of US$ 2,73 trillion in 2017 and economy is forecasted to grow at 7.3 per cent in 2017.

To improve infrastructure in villages, 204,000 Point of Sale (PoS) terminals have been sanctioned from the Financial Inclusion Fund by National Bank for Agriculture & Rural Development (NABARD).

The number of total bank accounts opened under Pradhan Mantri Jan Dhan Yojana (PMJDY) reached 333.8 million as on November 28, 2017.

Major Problems Faced by India's Banks

Problem # 1. Losses in Rural Branches:

Most of the rural branches are running at a loss because of high overheads and prevalence of the barter system in most parts of rural India.

Problem # 2. Large Over-Dues:

The small branches of commercial banks are now faced with a new prob-lem—a large amount of overdue advances to farm-ers. The decision of the former National Front Gov-ernment to waive all loans to farmers up to the value of Rs. 10,000 crores has added to the plight of such banks.

Problem # 3. Non-Performing Assets:

The commercial banks at present do not have any machinery to ensure that their loans and advances are, in fact, going into productive use in the larger public in-terest. Due to a high proportion of non-performing assets or outstanding due to banks from borrowers they are incurring huge losses. Most of them are also unable to maintain capital adequacy ratio.

Problem # 4. Advance to Priority Sector:

As far as ad-vances to the priority sectors are concerned, the progress has been slow. This is partly attributable to the fact that the bank officials from top to bot-tom could not accept nationalisation gracefully, viz., diversion of a certain portion of resources to the top priority and hitherto neglected sectors. This is also attributable to the poor and unsatis-factory loan recovery rates from the agricultural and small sectors.

Problem # 5. Competition from Non-Banking Financial Institution:

As far as deposit mobilisation is con-cerned, commercial banks have been facing stiff challenges from non-banking financial interme-diaries such as mutual funds, housing finance cor-porations, leasing and investment companies. All these institutions compete closely with commer-cial banks in attracting public deposits and offer higher rates of interest than are paid by commer-cial banks.

Problem # 6. Competition with Foreign Banks:

Foreign banks and the smaller private sector banks have registered higher increase in deposits. One reason seems to be that non-nationalised banks offer bet-ters customer service. This creates the impression that a diversion of deposits from the nationalised banks to other banks has probably taken place.

Problem # 7. Gap between Promise and Performance:

One major weakness of the nationalised banking system in India is its failure to sustain the desired credit pattern and fill in credit gaps in different sectors. Even though there has been a reorientation of bank objectives, the bank staff has remained virtually static and the bank procedures and prac-tices have continued to remain old and outmoded.

The post-nationalisation period has seen a widen-ing gap between promise and performance. The main reason seems to be the failure of the bank staff to appreciate the new work philosophy and new social objectives.

Problem # 8. Bureaucratisation:

Another problem faced by the commercial banks is bureaucratisation of the banking system. This is indeed the result of nationalisation. The smooth functioning of banks has been hampered by red-tapism, long delays, lack of initiative and failure to take quick deci-sions.

Problem # 9. Political Pressures:

The smooth work-ing of nationalised banks has also been hampered by growing political pressures from the Centre and the States. Nationalised banks often face lots of difficulties due to various political pressures. Such pressures are created in the selection of personnel and grant of loans to particular parties without considering their creditworthiness.

Road Ahead

Enhanced spending on infrastructure, speedy implementation of projects and continuation of reforms are expected to provide further impetus to growth. All these factors suggest that India's banking sector is also poised for robust growth as the rapidly growing business would turn to banks for their credit needs.

Also, the advancements in technology have brought the mobile and internet banking services to the fore. The banking sector is laying greater emphasis on providing improved services to their clients and also upgrading their technology infrastructure, in order to enhance the customer's overall experience as well as give banks a competitive edge.

India's digital lending stood at US$ 75 billion in FY18 and is estimated to reach US$ 1 trillion by FY2023 driven by the five-fold increase in the digital disbursements.

Conclusion

Indian banks have been regarded and included in the Brand Finance® Global Banking 500In the annual international ranking conducted by UK-based Brand Finance Plc, 20. Further as per the Brand Finance Study the State Bank of India (SBI) has become the first Indian bank to be ranked among the Top 50 banks in the world, capturing 36th rank. Through which the brand value of SBI in 2010 increased from US$ 1.5 billion in 2009 to US$ 4.6 billion.

Indian Banking Industry's growth has been more qualitative than quantitative which is expected to remain the same for the coming years. The projections of "India Vision 2017" prepared by the Planning Commission, also the Draft 10th Plan, the report forecasts that the pace of expansion in the balance-sheets of banks would be decelerating.

By the end of March 2010 the total assets of all scheduled commercial bank was estimated at Rs 40,90,000 crores. Which constitutes of about 65 % of GDP at current market prices as compared to 67 %in 2002-03. Banks assets were also expected to grow at an annual composite rate of 19.4 % during the rest of the year against the growth rate of 16.7 % that was between 1994-95 and 2017-19.

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