
Indian Banking Development – Challenges & Prospects

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ABSTRACT: *The economic reforms introduced by the Govt. of India about two decades ago have changed the landscape of several sectors of Indian economy. The Indian banking sector is of no exemption. This segment is going through major changes as a result of economic reforms. The role of banking industry is very vital as one of the leading and mostly essential service sector. Today in India the service sector is contributing nearly half of the Indian GDP and the banking is most popular service sector in India. This paper explains the changing banking scenario, the impact of economic reforms and analyses the challenges and opportunities of national and commercial banks. This article is divided in three parts. First part includes the preface and general scenario of Indian banking industry. The second part discusses the diverse challenges and opportunities faced by Indian banking industry. Third part includes the conclusion.*

Key words: *Banking, Reforms, LPG, New Products, Progress,.*

INTRODUCTION

India's banking sector has been expanding rapidly over the past years followed by the emergence of universal banking, higher economic growth, and globalisation.

The banking industry is considered to be the lifeline of an economy. It activates and sustains economic growth. "If we look at the statistics, India being one of the top ten economies of the world and with relatively lower domestic credit to GDP percentage provides great opportunity for the banking sector to grow", the KPMG-CII report on the banking sector has observed.

The Indian **banking sector has seen unprecedented growth** along with remarkable improvement in its quality of assets and efficiency since economic liberalisation began in the early 1990's. From providing plain vanilla banking services, banks have gradually transformed themselves into universal banks. **ATMs, Internet banking, mobile banking** and social banking have made "anytime anywhere banking" the norm now.

The biggest opportunity for the Indian banking system today is the Indian consumer. Demographic shifts and cultural shifts are changing the profile of the Indian consumer. This is leading to a growing demand for competitive banking services.

OBJECTIVE

The objective of this paper is to elucidate the present banking scenario and to study the challenges and opportunities of national and commercial banks in changing banking scenario.

METHODOLOGY

This paper is the outcome of a secondary data on Indian Banking Sector with special reference to Indian context. To complete this, annual reports, various books, journals and periodicals have been consulted, several reports on this particular area have been considered, and internet searching has also been done.

Progression of the Indian Banking Industry

The first bank in India, called The General Bank of India was established in the year 1786. The East India Company established The Bank of Bengal/Calcutta (1809), Bank of Bombay (1840) and Bank of Madras

(1843). The next bank was Bank of Hindustan which was established in 1870. These three individual units (Bank of Calcutta, Bank of Bombay, and Bank of Madras) were called as Presidency Banks. Allahabad Bank which was established in 1865, was for the first time entirely run by Indians.

In India, there are 26 public sector banks, 25 private sector banks, 43 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks, and 93,550 rural cooperative banks, in addition to cooperative credit institutions. Public sector banks control nearly 80% of the market, thereby leaving much smaller shares for its private peers.

The economic liberalisation in the early 1990s that prompted huge private sector investment led to a steady increase in the business of the banking sector. The credit off-take surged aided by a strong economic growth, rising disposable incomes, increasing consumerism and easier access to credit. Total credit extended by India's scheduled commercial banks (SCB) went up to Rs. 64,998 billion by 2014-15 from Rs.19,312 billion in 2006-07. Demand has grown for both corporate and retail loans; particularly for the services, real estate and consumer durables.

Aggregate deposits have grown nearly three and a half times during the same period from Rs. 26,119 billion in 2006-07 to Rs. 88,989 billion in 2014-15. Deposit growth has been mainly driven by strong growth in savings amid rising disposable income levels. Access to the banking system has also improved over the years due to persistent government efforts to promote banking-technology, and expansion in un-banked and non-metropolitan regions

Phases of Evolution of Indian Banking Industry

In the evolution of this strategic industry spanning over two centuries, massive developments have been made in terms of the rules governing it, the ownership composition, products and services presented and the technology employed. The entire progression can be divided into four distinct phases.

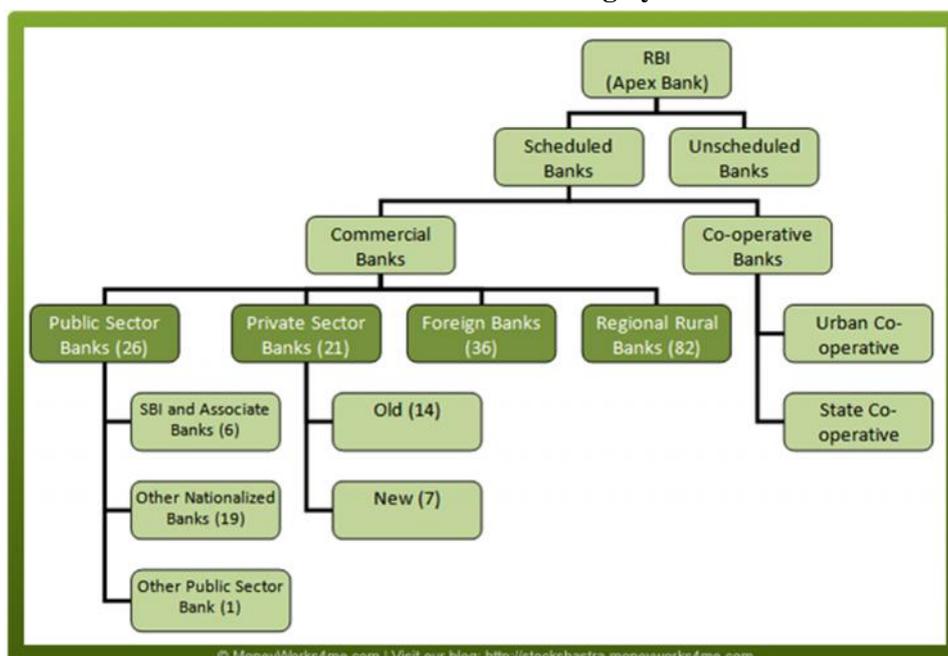
Phase I- Pre-Nationalization Phase (prior to 1955)

Phase II- Era of Nationalization and Consolidation (1955-1990)

Phase III- Beginning of Indian Financial & Banking Sector Reforms and Partial Liberalization (1990- 2004)

Phase IV- Period of Increased Liberalization (2004 onwards)

Structure of Indian Banking System



CHALLENGES AND OPPORTUNITIES

The Indian banking sector continues to face some structural challenges. In a country like India, we still has a huge number of people who do not have access to banking services due to broaden and uneven locations. But if we talk about those people who are availing banking services, their prospects are raising as the stage of services are increasing due to the emergence of Information Technology and competition. Since, foreign banks are performing in Indian market, the number of services accessible has improved and banks have laid stress on meeting the customer expectations.

Now, the existing situation has created various challenges and opportunity for Indian Commercial Banks. In order to encounter the general scenario of banking industry we need to understand the challenges and opportunities lying with banking industry of India.

a) **Indian Consumer in Rural Market**

The biggest opportunity for the Indian banking system today is the Indian consumer. India with a population of more than 120 crore people, Demographic shifts in terms of income levels and cultural shifts are altering the profile of the Indian consumer. This is leading to a growing demand for spirited, refined retail banking services.

The consumer represents a market for a wide range of products and services – he needs a credit to finance his house; an auto loan for his car; a loan for education, a credit card for purchases; a bank account; a pension plan for his retirement; a life insurance policy – the potentials are endless. And, this consumer does not reside just in India's top ten cities. In India, above 66% of population lives in rural areas. It is for this purpose, recently, ICICI Bank Ltd. merged with Bank of Rajasthan Ltd. in order to raise its attainment in rural market and market share significantly.

b) **Increased competition:**

The RBI and Government of India kept banking industry open for the participants of private sector banks and foreign banks. Due to this lowered entry barriers many new players have entered the market such as private banks, foreign banks, nonbanking finance companies, etc.

Profits of banks are being affected by increased competition. But increased competition has also resulted in increased efficiency, improved customer services and profitability in terms of returns on both equity and assets. Banks now have to continuously innovate their practices to stay ahead in the market. Increasing competition, however, might also persuade the banks to higher risk taking strategies.

c) **Innovations in Information Technology :**

Technology is the key to servicing all customer segments – offering convenience to the retail customer and operating efficiencies to corporate and government clients. The increasing sophistication, flexibility, and complexity of product and servicing offerings makes the effective use of technology critical for managing the risks associated with the business. Developing or acquiring the right technology, deploying it optimally, and then subsidizing it to the maximum extent is essential to achieve and maintain high service and efficiency standards while remaining cost-effective and delivering sustainable returns to shareholders. Early adopters of technology attain major competitive advantage. Managing technology is, thus, a major challenge for the Indian banking sector.

d) **Industrial Development:**

The developments in Indian industry and the integration of India with the global markets also offer innumerable opportunities to the banking sector. Companies and governments are ever more seeking high-quality banking services to improve their own operating efficiency. Companies seek to offer improved customer service and maximize shareholder returns and governments seek to improve the quality of open services. The internationalization of India offer banks the opportunity to service cross-border needs of Indian companies and India-linked needs of multinationals.

e) **High Transaction Costs:**

A major concern before the banking industry is the high transaction cost of carrying non-performing assets in their books. The growth lead to strains in the operational efficiency of banks and the accumulation of non-performing assets (NPA's) in their loan portfolios.

f) Management of Risks:

The growing competition increases the competitiveness between banks. But, present global banking scenario is seriously posing threats for Indian banking industry. We have by now witnessed the economic failure of some foreign banks. Ex. Lehmanbro's.

Al-Tamimi and Al-Mazrooei (2007) examined the risk management practices and techniques in dealing with different types of risk.

g) Financial inclusion:

Financial inclusion or inclusive financing is the delivery of financial services at affordable costs to sections of disadvantaged and low-income segments of society. In India, RBI has initiated several measures to achieve greater financial inclusion, like facilitating no-frills accounts and GCCs for small deposits and credit.

h) Appropriate HR Policies:

It has become imperative that for meeting the challenges and opportunities in future, there will be hugerequire for bringing about changes in the mindset of the human resource available within the banks. Training and development in updating the skills would be essential to face the emerging challenges. In a service segment like banking, human resources will occupy the crucial part for making the bank services. With the entry of new private banks and foreign banks, the method of hire-and-fire will be revisited. Security and age old practice of conducting traditional banking will undergo revolutionary change. Maintenance of best talent would be a trying exercise that banks will have to undertake and practice through robust reward and retention policy.

i) Customer Retention:

In today's Banking scenario, retaining the customer within our banking services is a very high task. The financial inclusion and setting up of new banks has made customers easily to embark into process of banking. Hence, the banks which can render high quality services can only retain the customers for longtime.

j) Product Re-Engineering Strategy:

The growth in disposable incomes, changing lifestyles, global changes and their impact on the economy will result in ever changing and diversified needs to the customers. Banks in future will have to recognize the dynamic needs of a changing society through detailed market surveys and structure innovative products so as to canalize the savings of the community and also to satisfy the credit requirements of various sectors of the economy.

k) Social, Ethical and Corporate Governance Aspects :

There are some banks, which proactively undertake the task to bear the social and ethical aspects of banking. This is a deal with for commercial banks to consider these aspects in their working. Apart from profit maximization, commercial banks are supposed to support those organizations, which have some social concerns.

l) Timely Technological Progression:

Already electronic transfers, clearings, settlements have reduced translation times. To face competition it is necessary for banks to absorb the technology and upgrade their services.

CONCLUSION

The competitive scenario in India is strong, with the landscape primarily dominated by government banks. Market entry at the country level is expected to be tough for new players due to the moderately consolidated nature of the industry and extremely high competition. The key challenges for the industry are to reduce NPAs, increase financial inclusion and raise capital for the Basel III compliance.

According to the top consulting firms, the growth of Indian banks, especially in the public sector, can be optimised through increasing productivity and efficient human resource management. Banks need to hire employees with both core and specialist skills, while simultaneously working to control attrition. Further, banks need to optimise the time and cost of performing non consumer activities with the help of special tools and revamping existing knowledge processes.

Sustained government support and a careful re-evaluation of existing business strategies can help the Indian banks achieve strong growth. Sustained government support and a careful re-evaluation of existing business strategies can set the stage for Indian banks to become bigger and stronger, thereby setting the stage for expansions into a global consumer base.

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