International Journal of Management and Economics ISSN: 2231 - 4687

Vol. I No. 19 November 2015 Impact factor: 2.25

Indian Banking Industry`s Performance in the Global context

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Introduction

The paradigm shift is taking place in delivering banking services by the bankers in the 21st century to its customers. Due to globalization, it becomes mandatory to all bankers to adhere the Corporate Governance in accordance with the amended Act. Enhancing the investor's confidence and encouraging competition among the banking industry is must in the recent years. Banking industries are coming under the direct scrutiny of the Reserve Bank of India. Hence, all the banking organizations have to comply with the regulatory requirements, apart from meeting the local community needs. Due to heavy inflow of foreign direct investment (FDI) from across the world, it become necessary to all the banks have to adhere the Corporate Governance strictly as per prevalence of law. A good Corporate Governance mechanism improves the health of the banking sector, thus enhancing national competitiveness.

The economic reforms have also generated new and powerful customers (huge Indian middle class) and new mix of players (public sector units, private banks, and foreign banks). The emerging competition has generated new expectations from the existing and the new customers. There is an urgent need to introduce new products. Existing products need to be delivered in an innovative and cost-effective way by taking full advantage of emerging technologies. As a consequence of competition, the managerial challenges include market segmentation, product positioning, innovative delivery channels, cross-selling, etc.

Services constitute a major portion of India's GDP with a 57 per cent share in GDP at factor cost (at current prices) in 2013-14 — an increase of 6 percentage points over 2000-01. Including construction, the share is 64.8 per cent. The CAGR of services sector GDP at 8.5 per cent for the period 2000-01 to 2013-14 has been higher than the 7.1 per cent CAGR of overall GDP during the same period. In 2013-14 the growth rate of the services sector at 6.8 per cent is marginally lower than in 2012-13. This is due to deceleration in the growth rate of the combined category of trade, hotels, and restaurants and transport, storage, and communications to 3.0 per cent from 5.1 per cent in 2012-13, despite robust growth of financing, insurance, real estate, and business services at 12.9 per cent. Construction, a borderline services inclusion.

STATEMENT OF THE PROBLEM

Banking industry is undergoing the paradigm shift from existing style of delivering services to new ways to cater the customers. It becomes necessary to every banking sector to study the opportunities and challenges in the changing globalised scenario. The ever increasing high end demand from the customers, to retain existing customers and to attract new customers is the challenges to the banking sector nowadays. This paper tries to analysis the foreign direct investment with sector-wise, especially in the banking sector and their performance in the globalised context.

REVIEW OF LITERATURE:

N.J Saleena (2013) in her article on Impact of FDI on Services Export: Evidence from India, Blue Ocean Research Journals, concluded that FDI has positively influenced the growth of services export in the Indian economy, after the liberalization period. During the post liberalization period the trade policies undertaken by the government (like the Foreign Trade Policy (2004-2009), the National Telecom Policy (NTP) etc.), the changing attitude of the government towards foreign direct investment has increased export opportunities has induced foreign investors to take advantage of India's comparative advantage in the Service Sector. Since services export is largely driven by information and communication technology, rapid advancement in information and communication technology (ICT) in India is likely to generate significant scope for export oriented services.

Jairaj Purandare (2010) Financial Services, Destination Banking Opportunities: Entry Strategy and the Road Ahead, Price water house Coopers, concluded that Banking is one of the strongest performing sectors in India with advances and deposit growing more than 20% in the last five years. The Return on Equity for the banking sector has been around 13% in the last four years with top performing banks having 18-20% as Return on Equity (RoE).

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OBJECTIVES OF THE STUDY:

➢To know country-wise and sector-wise flow of foreign direct investment to our country.

➢To study the share of foreign banks, public sector banks and private sector banks in the development of service sector in India.

➢To examine the India's GDP with other developing countries in the world.

➢To understand Indian bank's performance in terms of its cost and profit.

METHODOLOGY:

The study is based on secondary data. The source of data was collected from news papers, journals, annual reports and various websites from the internet.

HYPOTHESIS TESTED:

"The performance of nationalized banks was improved in terms of cost and profit while compared to other sector banks in the global context"

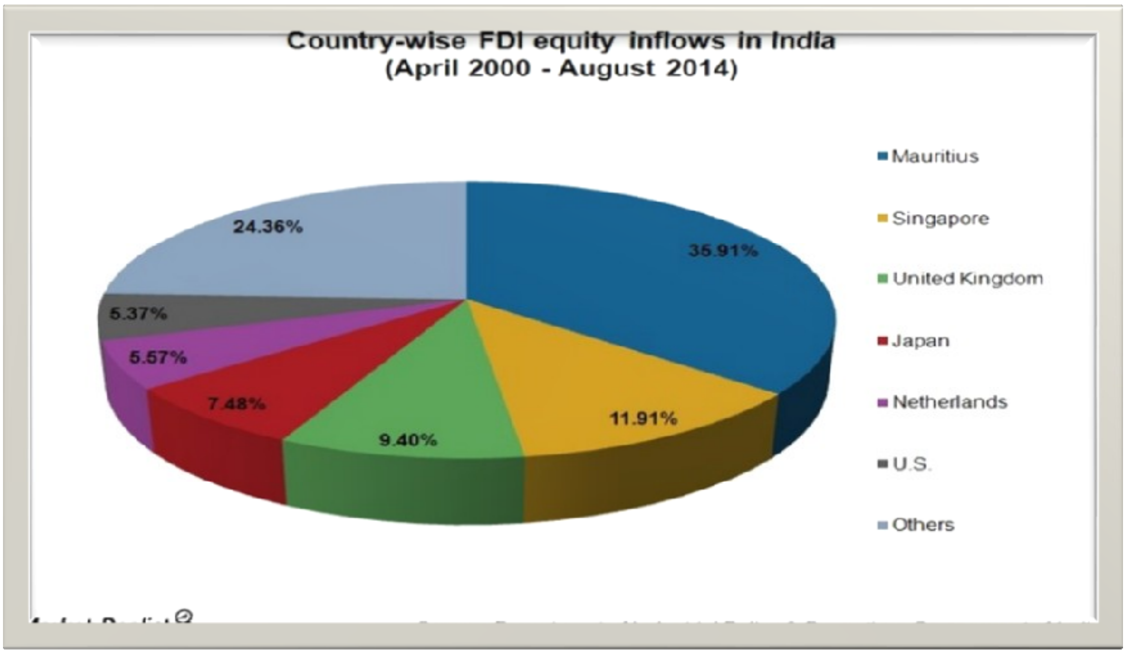
LIMITATIONS OF THE STUDY:

The study is based on secondary data. The study reveals about the performance of banking sector with respect to the flow of foreign direct investment from various countries. The area of the study is restricted to the performance of all banking sector in India.

OBSERVATIONS:

A healthy and developed country can easily attract more foreign direct investment across the world due to its economic soundness. Anybody in the world would definitely invest money by calculating the return from it. The return from the investment is little high in India compared to the other economy around the world.

<u>Figure No.1 Country – Wise FDI Equity inflows in India (April 2000 – August 2014)</u>

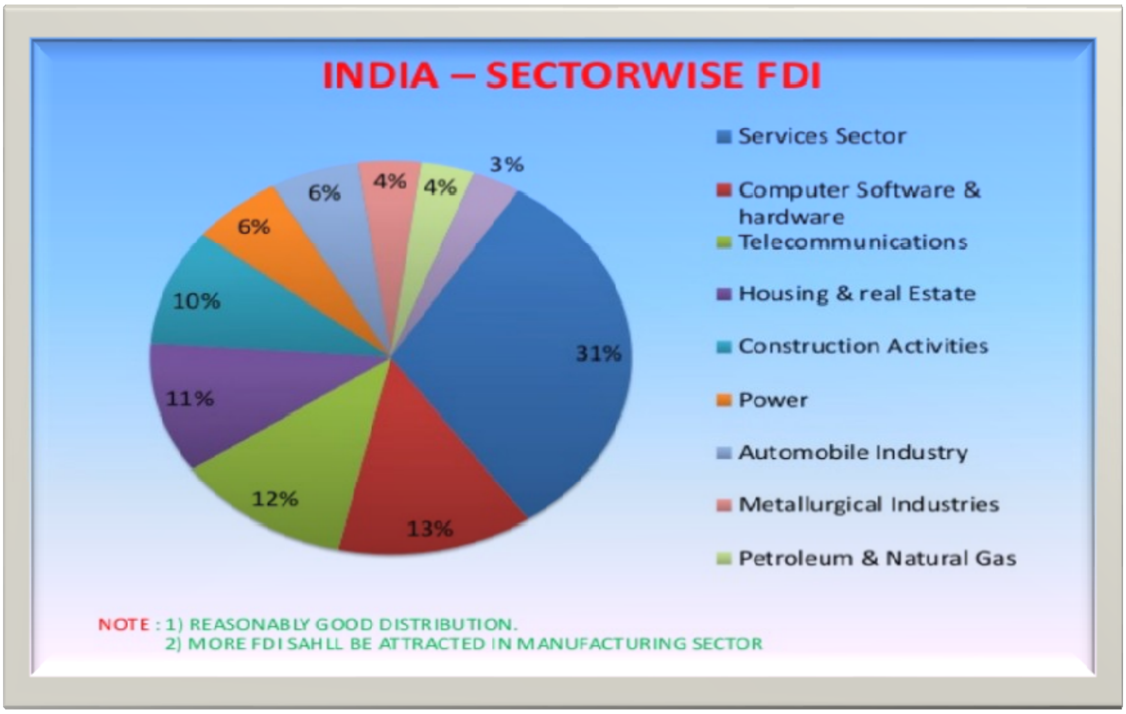


Source: Department of Industrial Policy & Promotion, Government of India

Figure no 1exhibits the flow of foreign direct investment over the years across the world. The analysis indicates that large part of FDI in India is contributed by fifteen countries which is. 185506.59 US $ million while remaining aprox. 11 per cent by rest of the world. Mauritius emerged as the most dominant source of FDI contributing 77,083.47 US$ million of the total investment in the country. It is because the

India has Double Taxation Avoidance Agreement (DTAA) with Mauritius. This (DTAA) type of taxation treaty has been made out with Singapore. So Singapore is second largest Investor of FDI inflow in India. The other major countries are U.K with a relative share 20,671.41 US$ million followed by Japan. While some countries like South Korea, Italy, Hong Kong has fewer shares in total FDI Inflow.

Figure No.2 Sector – Wise Flow of Foreign Direct Investment:



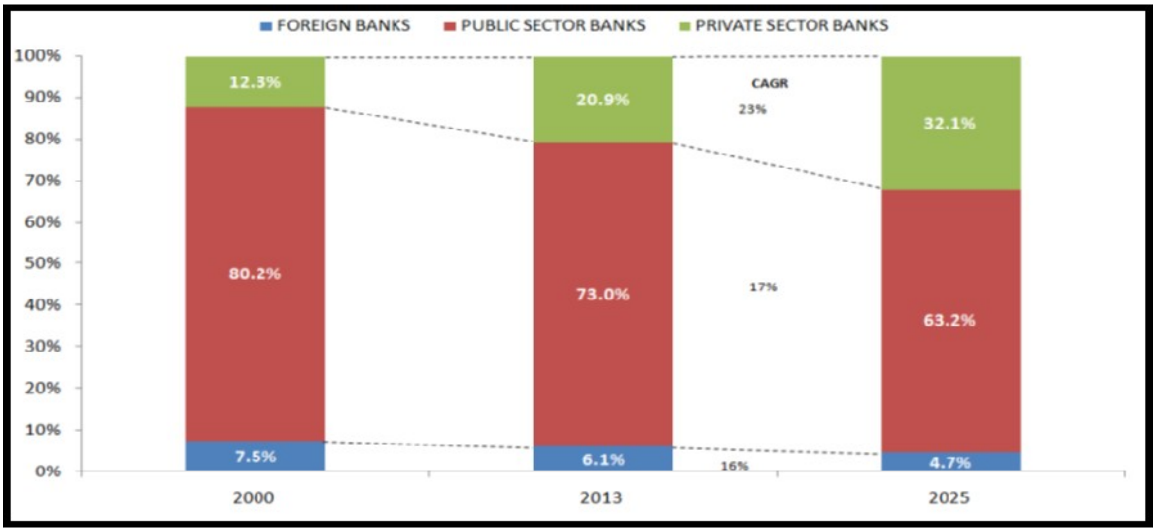
Source: http://theglobaljournals.com/gra/file.php?val=December_2013_1387275512_75066_11.pdf

Figure no2 depicts the inflow of foreign direct investment in India. From the above figure, it is noted that services sector has the highest inflows of foreign direct investment with 31 percent. Computer software & hardware with 13 percent, telecommunications with 12 percent, housing & real estate with 11 percent, construction activities with 10 percent, power sector with 6 percent, automobile sector with 6 percent and 4 percent each from metallurgical industries and petroleum and natural gas sector has the inflow of foreign direct investment in India. It shows that services sector has the potential to attract more foreign direct investment from abroad. Among the services sector banking industry is the top most priority to the foreign investors.

Market share of Indian Banking Sector:

Indian banking sector has undergone tremendous changes after nationalization and even in the post reform period. It is understood that, before nationalization, private sector banks and after nationalization, public sector banks were dominated in Indian economy. Since last two decades, the scenario has changed due to the policy adopted by the central governments. It leads to allow foreign banks as well as new private banks in the banking sector. Due to LPG, again the foreign players were started coming and doing more business along with the private sector banks in India.

Figure No.3.Estimates of market share based on linear projection



Source: Report of the Committee to Review Governance of Boards of Banks in India May 2014

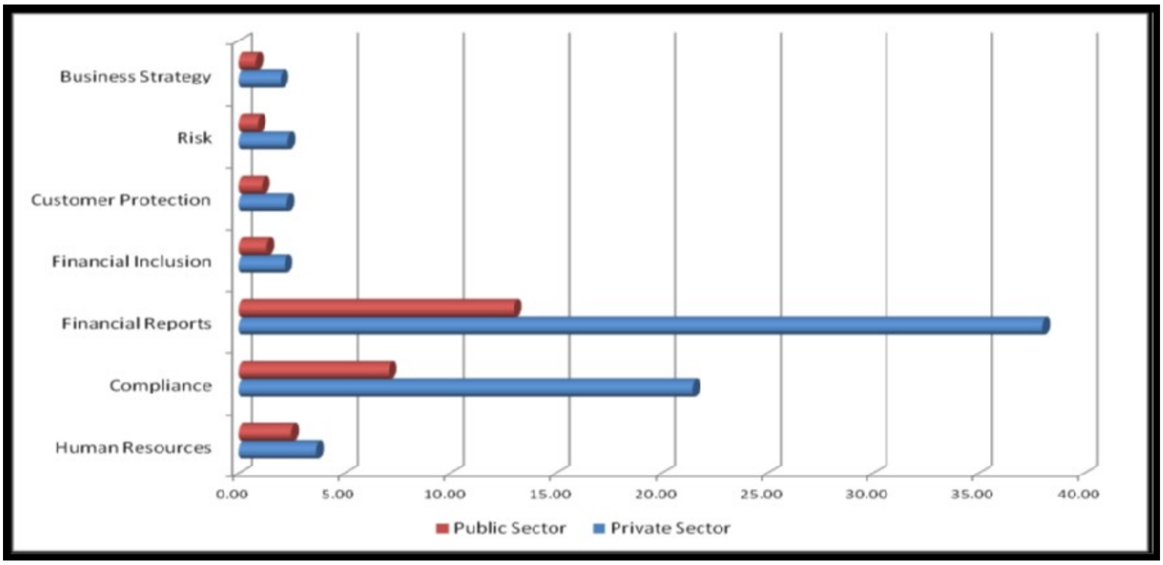
The above figure portrays the banking sector's market share in different period. Market share changes are visible on account of differences in the compounded annual growth rate (CAGR) in assets across these categories for the period 2000-13. It is projected in the year 2025, the market share of private sector banks (with comparison of CAGR) would be around 32.1 percent which is almost more than 260 percent growth from the year 2000 to 2025. At the same time the growth (CAGR) of public sector banks would be estimated to be 63.2 percent which is very less from the year 2013 (73.0%). Thus, in the coming years, it is to be proved that private banking sector would play vital role in the Indian economy. At the same period, foreign banks would be losing their market share at all time high.

There are seven critical themes which bank boards are typically concerned with: business strategy, risk mitigation, financial reports and their integrity, compliance, customer protection, financial inclusion, and human resource related issues. There are other important matters too which concern bank boards, such as operations. But it is arguable that asserting the competitive positioning of a public sector bank appears to require its board to provide greater focus on the seven critical themes listed.

Category	Description
Business Strategy	Bank and business strategy; development of new products; competitiveness of individual businesses; business reviews in relation to targets.
Risk	Policies concerning credit, operational, market, liquidity risks; assessing the independence of the risk function.
Financial Reports and their integrity	Detailed scrutiny of quarterly and annual financial results; NPA management and reported NPA and provisioning integrity.
Compliance	Regulatory requirements; adherence to RBI and SEBI norms; observations from the annual financial inspection by RBI, and from the Long Form Audit Report; review of decisions in previous minutes of meetings, and key decisions within subsidiaries; review of action taken reports; appointments to board committees.
Customer Protection	Mis-selling, particularly third-party products; laying down the appropriateness of products to different customer segments; understanding the broad trends

	and concentration in the growth of customer grievances and their resolution.
Financial Inclusion	Review of priority sector lending; payments for the disadvantaged; deposit mobilization from weaker sections; support to microfinance institutions; and other issues.
Human Resources	Appointments and approvals of directors, perks and perquisites for employees, incentive schemes for employees, promotion policies for employees, training and skill development of employees.

FigureNo.4. Average Number of Issues Tabled:



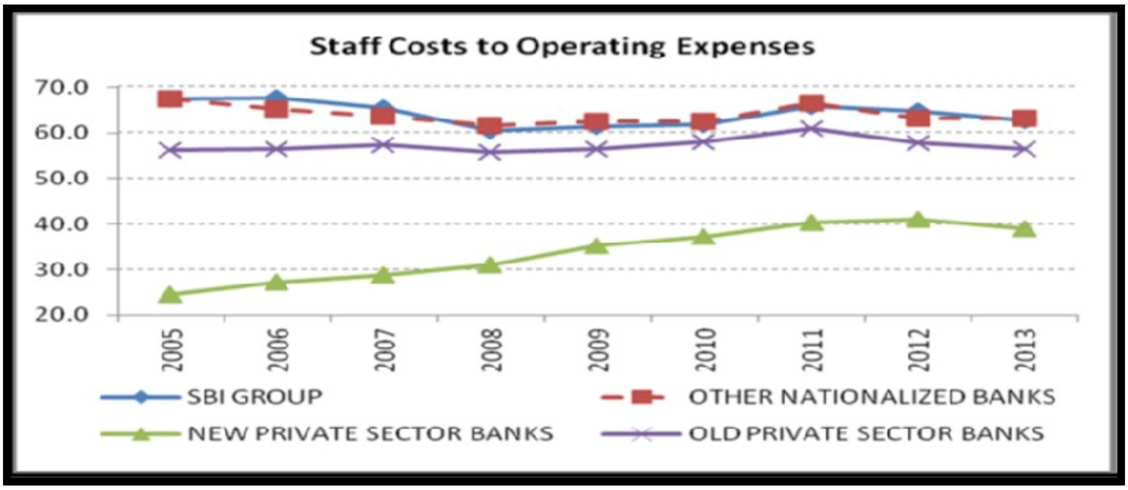
Source: Report of the Committee to Review Governance of Boards of Banks in India May 2014

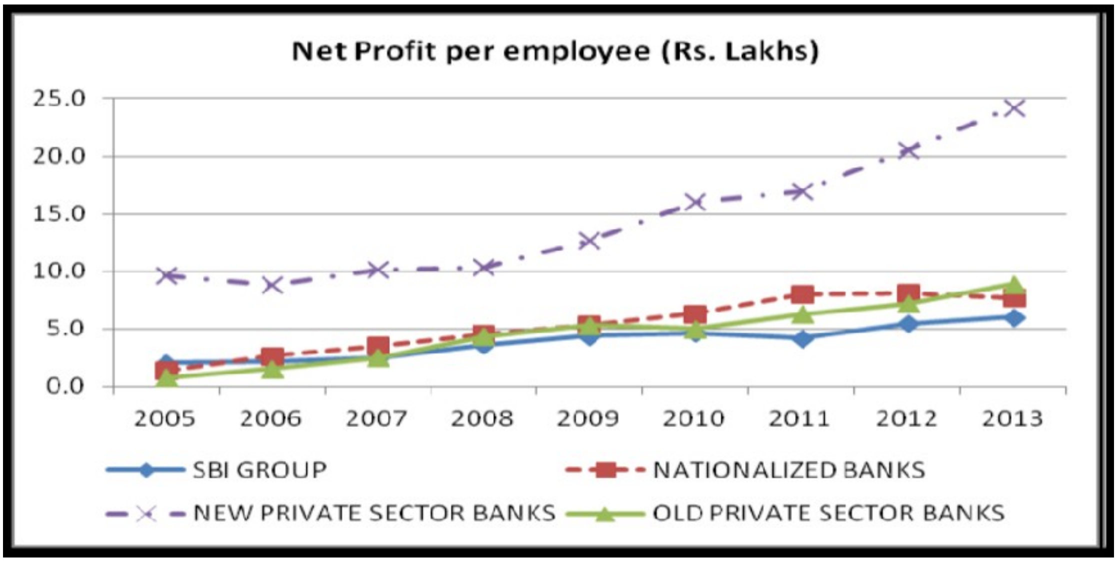
For banks, business strategy and risk mitigation are particularly crucial, and in terms of data furnished by the banks it appears that in both private sector and public sector bank board's there is (on average) inadequate focus on these compared to other issues. On average, both in private sector and public sector bank board's only 6 per cent of the issues tabled include those pertaining to business strategy and risk mitigation though private sector bank boards to do somewhat better with respect to the number of issues tabled in these two categories.

Because they are so highly leveraged, banks (more than non-financial enterprises) need to synchronies their focus on these two themes, with the balance between them varying in different phases of the business cycle. In business cycle downturns, particularly, risk mitigation also needs to be watchful of tail risks which could imperil bank solvency.

Figure no. 5 &6 expresses the performance of the banking sector in terms of cost and net profit over the period of time. It is observed from the figures that the staff cost to operating expenses and net profit per employee's point of view that, the new private banking sector playing very vital role in the Indian banking sector. There are other ways in which productivity differences are seen to be reflected in lower profitability. As far as productivity is concerned, the low cost per employee and the maximum profit per employee is greater with the new private sector banks. It is understood that the new private sector banks (corporate entities) would play very important role in the coming years.

Figure No.5&6. Banking Sector Performance (Operating cost and Profit)





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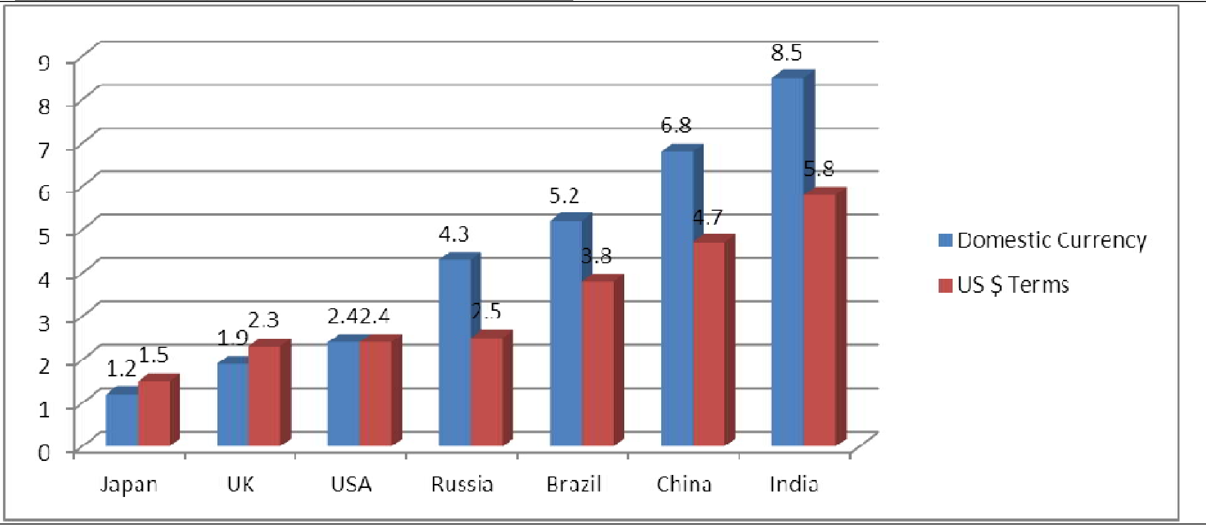
OPPORTUNITIES:

The major opportunity for the Indian banking system today is the Indian consumer. Demographic shifts in terms of income levels and cultural shifts in terms of lifestyle aspirations are changing the profile of the Indian consumer. This is and will be a key driver of economic growth going forward. The Indian consumer now seeks to fulfill his lifestyle aspirations at a younger age with an optimal combination of equity and debt to finance consumption and asset creation. This has witnessed the growing demand for competitive, sophisticated retail banking services. The consumer represents a market for a wide range of products and services like housing finance ,vehicle finance, a credit card for ongoing purchases; a bank account; a long-term investment plan to finance his child's higher education; a pension plan for his retirement; a life insurance policy – the possibilities are endless. Hence, the level of awareness has increased in all the places like cities, towns, and villages. Marketers are already tapping this potential market with the help of tie-up between local banks in those regions to give the solution.

Figure No.7 Projected GDP growth 2007 - 2050



Source: PwC Research

Figure no 7.exhibits the projected growth of GDP between 2007-2-50. According to the research analysis, India's middle class segment is steadily rising and with 250-300 million people in this segment, it is expected to double in the next two decades. Compared to other economies, India has a relatively young population with around 35% of the population falling in this category. The median age of the Indian population is 25.5 years which indicates that India is in a good position to benefit from its demographic dividend. The Indian economy is opening up at a steady pace. The quantitative restrictions on imports ended in 2001, opening up the economy to foreign businesses, especially in consumer goods. Gradually, barriers to trade and investment are coming down. The peak customs duty rate was reduced to 10% in 2008 (for non-agricultural and other specified goods). In August 2009, India signed Free Trade Agreements with the Association of Southeast Asian Nations (ASEAN) nations and Korea, which is expected to boost trade.

Table No.1Financial Years Wise FDI Flow From 2000-01 to 2013-14

Financial Years 2000-01 to 2013-14 (up to November, 2013)			
Sr.No	Financial Year (April To March)	Total FDI flow in US$ Million	Total FDI Flows % Growth Over Previous
1	2000-01	4,029	-
2	2001-02	6,130	(+) 52 %
3	2002-03	5,035	(-) 18 %
4	2003-04	4,322	(-) 14 %
5	2004-05	6,051	(+) 40 %
6	2005-06	8,961	(+) 48 %
7	2006-07	22,826	(+) 146 %
8	2007-08	34,843	(+) 53 %
9	2008-09	41,873	(+) 20 %
10	2009-10	37,745	(-) 10 %
11	2010-11	34,847	(-) 08 %
12	2011-12	46,556	(+) 34 %
13	2012-13	36,860	(-) 21%
14	2013-14 (P) (Apr-Oct, 2013)	18,934	-
Cumulative total (April, 2000 to October, 2013)		309,012	-

Source: DIPP, Federal ministry of commerce and industry, Govt. of India

Table no 1 depicts that flows of FDI received in India during April 2000 to October 2013 i.e. 309,012 US$ million. From the year 2000 to 2002 FDI inflow in India has shown a increasing trend. This may be the result of Foreign Exchange Management Act (FEMA) which is introduced in 1999. Further it follow negative trend up to period 2003-2004. But from the year 2004-05 to 2008-09 investment into India once again start growing. The highest FDI inflows growth in the country in 2006-2007 year was 146%. Further, FDI inflows rose by 34 % to US$ 46,556 million during 2011-12. Last year April 2012-13 has shown negative growth rate i.e. -21% to US$ 36,860 million while the cumulative amount of FDI equity inflows from April 2000 to October 2013 stood at US$ 309,012 billion, according to the latest data released by the Department of Industrial Policy and Promotion (DIPP).

A key driver of growth is innovation that surprises and delights consumers with new, differentiated, and relevant benefits. India will shortly become home to the second largest number of elderly persons in the world. The population of our elderly, at present estimated at 76

Million, is expected to increase to 100 million in 2013. Therefore, banks should focus on unmet financial needs of the pensioners and senior citizens.

CHALLENGES:

- Technology is the weapon for growth of any sector in the present world. Without which no sector can survive and succeed. The clear indication is that the growth can happen with the help of technology only. This becomes the biggest challenge to the banking industry to bring the services to all needy people with simplest way.
- Changing needs of customers is the second biggest challenge to the banking industry. Due to ever changing needs of the customers, bankers have to have a continuous market research and to study changing behavior of the customers. .
- Coping with regulatory reforms is another challenge to the banking industry. Rules and regulations have been changing time to time. Bankers have to change the rules and make it transparent to their customers.
- Maintaining high quality assets become one of the great challenges to the banking industry. Maintaining the low non-performing assets is always a key driver for the growth of the banking industry.
- Sustaining healthy bottom lines and increasing shareholder value the structure of Indian banking system may be expected to undergo a transformation, the main drivers of which will be consolidation, convergence, and technology. This will also reduce overcapacity in the Indian banking system and result in banking concentration. The changes in structure would also impact on the banking strategy.
- Banks would grow out of their narrow focus on banking services to become financial service providers.
- The one-stop-shop approach would enable them to provide, besides banking services, a host of other financial products, both to the retail as well as corporate customers.
- The other key challenges for the Indian economy are: Inflation, Inclusive growth, infrastructure development, withdrawal of stimulus.

HYPOTHESIS TESTING:

From the study, it is been concluded that the estimates of market share based on linear projection is concerned, (figure no 3) private sector would play vital role in the Indian economy. Also, figure no 5 & 6 shows that the new private sector bank's productivity is higher than that of other banks. Thus, the hypothesis is that "The performance of nationalized banks was improved in terms of cost and profit while compared to other sector banks in the global context" is rejected.

As mentioned earlier in this paper, the public sector has to focus in the areas of business strategy, risk, financial reports and their integrity, compliance, customer protection, financial inclusion and human resources to overcome the present difficulties and to retain the position in the banking sector in India.

CONCLUDING REMARK:

The research is exploratory and analytical. It is observed from the study is that the country – wise FDI equity inflows in India from Mauritius was higher than other countries in the world. With respect to sector – wise inflow of FDI is concerned; services sector has received 31 percent, which is the highest in India. As for as performance of nationalized banks in respect of market share and the cost benefit analysis are concerned, nationalized banks have been consistently decreasing and other hand new private sector banks have been increasing over the period of time. The study also proved that the cost and profit analysis is concerned, new private sector bank's productivity is better than other banks. As far as the projected growth is concerned, India would become the number one position with 8.5 in terms of Domestic currency and 5.8 in terms of US $ in the year 2050.

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